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International Accounting Standards Board
Columbus Building, 7 Westferry Circus
Canary Wharf, London, E14 4HD
United Kingdom

Comments on the Discussion Paper *Business Combinations under Common Control*

To the IASB Board Members:

The Japanese Institute of Certified Public Accountants ("we" and "our") appreciates the continued efforts of the International Accounting Standards Board on this project, and welcomes the opportunity to comment on the Discussion Paper *Business Combinations under Common Control* ("DP").

When selecting the measurement method, we agree with the Board's preliminary view that neither the acquisition method nor a book-value method should be applied to all business combinations under common control, given that there are a wide variety of transactions related to business combinations under common control. As an alternative, we propose that the acquisition method should be applied to business combinations under common control only when the receiving company's shares are traded in a public market, and a book-value method should be applied to all other cases.

Provided that non-controlling shareholders of the receiving company acquire an ownership interest in the economic resources of the transferred company, we believe, in principle, the acquisition method should be applied if business combinations under common control are similar to business combinations covered by IFRS 3 (paragraph 2.20 of the DP). In such cases, business combinations under common control should affect a substantial or sufficient number of independent non-controlling shareholders of the receiving company, none of which are related parties of the company. In other words, we suggest the acquisition method should be applied only when the receiving company's shares are traded in a public market. This is because minimum listing requirements or capital market regulations for public trading in many jurisdictions typically suggest that the existence of the above-mentioned non-controlling shareholders is assured (paragraph 2.39 of the DP).

In general, publicly traded companies have a good governance with an expectation that the consideration transferred from the receiving company would not differ significantly from an arm's length price of the transferred company. Further, in such cases, we expect the application of the acquisition method would not be so costly or burdensome in practice, assuming an appropriate acquisition process would take place, including a fair evaluation of assets and liabilities. On the other hand, if it is a privately held receiving company, the controlling party would have a greater control, indicating that the situation for non-controlling shareholders of the receiving company could be different under such circumstances. In such cases, we think the optional exemption from the acquisition method could be burdensome as a procedure, under which the book-value method instead of the acquisition method is permitted to be used if the receiving company has informed all of its non-controlling shareholders that it proposes to use a book-value method and they have not objected. Thus, from a reasonable cost–benefit trade-off perspective, we suggest a book-value method should also be applied to all privately held receiving companies, not just when all of non-controlling shareholders of the receiving company are related parties of the company.

Please find our comments to the questions raised in the DP, in the following pages.

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?

Comment:

We agree with the Board's preliminary view only if the following is further considered:

We understand that the scope of the DP covers only "business combinations" under common control, and other transactions are basically outside the scope of the project. However, there are a number of similar transactions under common control that fall outside the scope. Given that accounting requirements applied to such transactions are not always specifically provided, we see diversity in practice for certain transactions, including an acquisition of assets under common control that are not regarded as a business and a transfer of an investment in an associate or a joint venture among entities under common control. Moreover, there could be other practical issues not directly covered within the project that need to be further addressed, such as the following: the accounting treatment for a transferring company, whether or not it should mirror that of the receiving company; the reporting of a receiving company in its separate financial statements; and the accounting for merger transactions among entities under common control.

Although the scope of the project seems to be too narrow to cover a broad variety of practical issues, we can say that the project is currently in the first phase where discussions are focused on simple and straight-forward transactions to establish some kind of principles. That said, we suggest the Board should expand the scope to cover broader issues at the next phase of the project.

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?

Comment:

Comment to Question 2(a)

We agree that neither the acquisition method nor a book-value method should be applied to all business combinations under common control, given that there are a wide variety of transactions related to business combinations under common control. Especially, always applying the acquisition method does not seem to be practical as a requirement.

Comment to Questions 2(b) and 2(c)

We conditionally agree with the principle that 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. We could suggest the following as an alternative proposal:

Provided that non-controlling shareholders of the receiving company acquire an ownership interest in the economic resources of the transferred company, we believe the acquisition method should be applied if business combinations under common control are similar to business combinations covered by IFRS 3 (paragraph 2.20 of the DP). In such cases, business combinations under common control should affect a substantial or sufficient number of independent non-controlling shareholders of the receiving company, none of which are related parties of the company. In other words, we suggest the acquisition method should be applied only when the receiving company's shares are traded in a public market. This is because minimum listing requirements or capital market regulations for public trading in many jurisdictions typically suggest that the existence of the above-mentioned non-controlling shareholders is assured (paragraph 2.39 of the DP).

Therefore, we suggest the acquisition method should be applied to business combinations under common control only when the receiving company's shares are traded in a public market, and a book-value method should be applied to all other cases. In general, publicly traded companies have a good governance with an expectation that the consideration transferred from the receiving company would not differ significantly from an arm's length price of the transferred company. Further, in such cases, we expect the application of the acquisition method would not be so costly or burdensome in practice, assuming an appropriate acquisition process would take place, including a fair evaluation of assets and liabilities.

On the other hand, when the receiving company's shares are not traded in a public market (i.e. a privately held receiving company), the controlling party would have a greater control, indicating that the situation for non-controlling shareholders of the receiving company could be different under such circumstances. In such cases, we think the optional exemption from the acquisition method could be burdensome as a procedure, under which the book-value method instead of the acquisition method is permitted to be used if the receiving company has informed all of its non-controlling shareholders that it proposes to use a book-value method and they have not objected. Thus, from a reasonable cost–benefit trade-off perspective, we suggest a book-value method should also be applied to all privately held receiving companies, not just when all of non-controlling shareholders of the receiving company are related parties of the company.

Selecting the measurement method
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?

Comment:

We agree with the Board's preliminary view for (a) and (b)(ii). However, we do not agree with (b)(i) and would like to suggest the following instead:

Provided that non-controlling shareholders of the receiving company acquire an ownership interest in the economic resources of the transferred company, we believe the acquisition method should be applied if business combinations under common control are similar to business combinations covered by IFRS 3 (paragraph 2.20 of the DP). In such cases, business combinations under common control should affect a substantial or sufficient number of independent non-controlling shareholders of the receiving company, none of which are related parties of the company. In other words, we suggest the acquisition method should be applied only when the receiving company's shares are traded in a public market. This is because minimum listing requirements or capital market regulations for public trading in many jurisdictions typically suggest that the existence of the above-mentioned non-controlling shareholders is assured (paragraph 2.39 of the DP).

Therefore, we suggest the acquisition method should be applied to business combinations under common control only when the receiving company's shares are traded in a public market, and a book-value method should be applied to all other cases. In general, publicly traded companies have a good governance with an expectation that the consideration transferred from the receiving company would not differ significantly from an arm's length price of the transferred company. Further, in such cases, we expect the application of the acquisition method would not be so costly or burdensome in practice, assuming an appropriate acquisition process would take place, including a fair evaluation of assets and liabilities.

On the other hand, when the receiving company's shares are not traded in a public market (i.e. a privately held receiving company), the controlling party would have a greater control, indicating that the situation for non-controlling shareholders of the receiving company could be different under such circumstances. In such cases, we think the optional exemption from the acquisition method could be burdensome as a procedure, under which the book-value method instead of the acquisition method is permitted to be used if the receiving company has informed all of its non-controlling shareholders that it proposes to use a book-value method and they have not objected. Thus, from a reasonable cost–benefit trade-off perspective, we suggest a book-value method should also be applied to all privately held receiving companies, not just when all of non-controlling shareholders of the receiving company are related parties of the company.

Selecting the measurement method
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?

Comment:

Comment to Question 4(a)

We agree with the Board's preliminary view that the optional exemption from the acquisition method should not be available for publicly traded receiving companies. That said, as commented above at Questions 2 and 3, we suggest the acquisition method should be applied to business combinations under common control only when the receiving company's shares are traded in a public market, and the book-value method should be applied to all other cases.

Comment to Question 4(b)

We agree that the related-party exception to the acquisition method should not apply to publicly traded receiving companies. That said, as commented above at Questions 2 and 3, we suggest the acquisition method should be applied to business combinations under common control only when the receiving company's shares are traded in a public market, and the book-value method should be applied to all other cases.

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?

Comment:

Comment to Question 5(a)

We agree that the Board should not develop a new requirement for the receiving company to identify, measure and recognise a distribution from equity due to its complexity. Further, such information might not be useful enough to be provided at a cost justified by the benefits of that information.

Comment to Question 5(b)
We do not agree with the Board's preliminary view. The acquisition method should be applied to business combinations under common control only when the receiving company's shares are traded in a public market. As publicly traded companies are generally expected to have a good governance with an expectation that an amount paid as for consideration in such cases would not differ significantly from an amount that would have been paid to an unrelated party in an arm's length transaction, the accounting treatment for the acquisition method should follow that of IFRS 3. We believe applying certain disclosure requirements should be able to address the concern described in paragraphs 3.6 and 3.19 of the DP, saying that the amount of consideration paid in business combinations under common control may include an additional component other than consideration paid to an unrelated party in an arm's length transaction.

Comment to Question 5(c)
We do not agree with developing any other special requirements because we suggest the acquisition method should be applied to business combinations under common control only when the receiving company's shares are traded in a public market and the accounting treatment should follow that of IFRS 3.

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?

Comment:
The measurement should not be limited to using the transferred company's book values due to the following reasons:

- In certain cases, such as when an intermediate parent company acquires a subsidiary's business, book values per the parent's consolidated financial statements might better reflect the latest value of acquired assets.

- If a business is subject to a transfer but no financial statements are prepared for the business in the past, it is uncertain as to how book values of the 'transferred company' (or business) can be obtained. In such cases, we might be able to refer to book values originally recorded in the transferring company's financial statements, but it is currently not clarified in the DP.
- Financial statements of the transferred company might not be prepared based on IFRS. In such cases, it may cause undue cost for the company preparing IFRS-based financial statements only for the purpose of pursuing the transaction.

Applying a book-value 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?

Comment:

We agree with the Board's preliminary view based on the reasons described in paragraphs 4.28, 4.34 and 4.42 of the DP.

Applying a book-value method
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?

Comment:
We agree with the preliminary view because an approach that requires the difference to be segregated into components could be costly and complex to apply (paragraph 4.46 of the DP).

Applying a book-value method
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?

Comment:
We conditionally agree with the Board's preliminary view.

We agree that when business combinations under common control are similar to business combinations covered by IFRS 3, transaction costs should be recognised as expenses in the period they are incurred. However, for business combinations under common control that are not similar to business combinations covered by IFRS 3, the Board should consider that transaction costs may include components other than consideration based on an arm's length transaction. When applying a book-value method to a business combination under common control that are not similar to business combinations covered by IFRS 3, we should be aware that the Board's conclusion in paragraph BC366 of IFRS 3 is not always applicable, which says that 'acquisition costs are not part of the fair value exchange between the buyer and seller for the business' and 'rather, they are separate transactions in which the buyer pays for the fair value of services received.'

Further, acquisition-related costs may include unavoidable costs of the investment in a business with an intent to recover such costs through post-acquisition operations of the business. When measuring assets and liabilities at historical costs applying a book-value method, we believe such acquisition-related costs should be included as part of the investment, because the accounting treatment aligns with the measurement of other non-current assets and inventories at the time of acquisition.

We highly recommend the Board should take this into account and give careful consideration when developing the new standard.

Applying a book-value method
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?

Comment:

We agree with the preliminary view based on the Board's conclusion that the benefits of information provided by a retrospective approach may be limited and may not outweigh the costs of providing that information (paragraph 4.62 of the DP).

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?

Comment:

Comment to Question 11(a)

We basically agree with the Board's preliminary view that the receiving company should be required to comply with the disclosure requirements in IFRS 3. We also agree that any improvements to disclosure requirements resulting from the Discussion Paper *Business Combinations—Disclosures, Goodwill and Impairment* (IFRS 3 Discussion Paper) should also be considered. That said, we would like to emphasise the importance of carefully taking the feedback on the IFRS 3 Discussion Paper into consideration when holding deliberations on disclosure requirements for business combinations under common control, including those raised by JICPA as outlined below (see detail of our comment letter issued on December 10, 2020):

・Strategic rationale, management's objective for the acquisition and subsequent performance of the acquisition

Proposed disclosure items in the IFRS 3 Discussion Paper include certain information that we think should be provided outside the financial statements. For example, it is still not yet certain as to whether information on market share and retention of staff, which is non-financial metrics used by management (paragraph 2.16(d) of the IFRS 3 Discussion Paper), meets the definition of 'Notes' set forth in the existing IAS 1 and should be presented as such in the financial statements in accordance with paragraph 112 of IAS 1. That said, JICPA has recommended the IASB should clarify items to be provided outside the financial statements, such as part of management commentary, before requiring companies to disclose information that should be included as notes to the financial statements.

We assume metrics used by management to monitor progress in meeting objectives include information about thresholds used by management for the selected metrics in determining whether or not an acquisition is successful, such as 'reaching the market share of 25% for Product Y by Year 202X.' We have raised concerns that information on management's assessment about those thresholds as well as year-end progress levels indicating management's assessment on how successful the company is towards the targeted threshold to meet its objectives could represent information that is not only unsuitable as notes to the financial statements, but also hard for auditors to audit the reasonableness.

・Pro forma information for the current period as though the acquisition date had been at the beginning of the annual reporting period

We have pointed out in our comment letter that the issue of auditability has already been raised under the current disclosure requirements, and therefore, a careful consideration should be given on expanding the scope of disclosures to be made as notes to the financial statements.

The IASB proposes the term 'profit or loss' in the pro forma information should be replaced with the term 'operating profit before acquisition-related transaction and integration costs' not only for information of the combined entity (paragraph 2.51(q)(ii) of the IFRS 3 Discussion Paper), but also for that of the acquiree since the acquisition date (paragraph 2.51(q)(i) of the IFRS 3 Discussion Paper). However, according to paragraph 53 of IFRS 3, acquisition-related transaction costs represent costs the acquirer incurs, meaning they are costs that would not have been incurred by the acquiree. Nonetheless, the proposal sounds as if such costs were included in the operating profit of the acquiree's business. As we think it is only creating confusion, we have recommended the IASB should modify the proposal as appropriate.

Disclosure requirements
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?

Comment:

We agree with the preliminary view.

<Book value disclosed under a book-value method>

As we commented above at Question 6, when applying a book-value method, we recommend the measurement should not be limited to using the transferred company's book values. For example, in some cases, book values in the parent's consolidated financial statements could be more appropriate. Based on our recommendation, we propose information should be disclosed on which book values are used when applying a book-value method.

Yours faithfully,

Takako Fujimoto
Executive Board Member － Business Accounting Standards and Practice/Corporate Disclosure
The Japanese Institute of Certified Public Accountants