Opinion Issued by the Accounting Standards Board
Method of Accounting for a Common Control Transaction under Accounting Standard 'Accounting for Common Control Transactions'

Brief facts of the enquiry:

The enquiry is primarily with respect to a common control transaction entered into by group of companies in which one listed Company namely XYZ Company Ltd (here-in-after referred to as 'the acquiring Company'/ XYZ Company), purchased a cereal business unit from ultimate parent of the Group namely ABC Foundation. This transaction falls within the ambit of common control transaction as the controlling party (Ultimate Parent) of the acquiring Company remains same before and after this transaction. The common control transactions are required to be accounted for as per requirements of Accounting Standard 'Accounting for Common Control Transactions' issued by SECP vide S.R.O. 53 (I)/2022 dated January 12, 2022.

The paragraphs 18-20 of the Standard describe the accounting of a Common Control Transaction of the "Receiving Entity" as follows:

a. If the non-controlling interest (NCI) is insignificant (less than 25%) in the receiving entity, the accounting shall be done by applying the 'Predecessor method';

b. If the NCI is significant (25% or above), the entity may elect to apply 'Predecessor method' or 'Acquisition method' to account for the common control transaction in its financial statements.

As per information received, there is a difference of opinion between the statutory auditors of the XYZ Company and management of XYZ Company as to what is meant by Non-controlling interest as referred to in paragraph 18 to 20 of the accounting standard 'Accounting for Common Control Transactions'. The statutory auditors are of the view that term 'non-controlling interest' used in paragraph 18-20 of the Accounting Standards means direct non-controlling shareholders of XYZ Company and does not require to include indirect non-controlling shareholding in XYZ Company of other group companies which carry shareholding in XYZ Company. The management of XYZ Company, however, is of the view that non-controlling interest means all shareholding of all direct and indirect non-controlling shareholders of XYZ Company. In case auditors' view is correct, XYZ Company is required to follow predecessor method of accounting for transaction of purchase of business unit from Ultimate Parent ABC Foundation as required under paragraph 18 of the Accounting Standard.

As per management of XYZ Company, the equity attributable to ultimate parent is the sum of direct ownership and effective indirect ownership. Therefore, the effective shareholding of Ultimate Parent ABC Foundation in XYZ Company is 39%, resulting in an NCI of 61%.

However, the auditors of XYZ Company are of the view that the NCI shall be determined based on the absolute shareholding in XYZ Company by the Overall Group companies instead of effective shareholding. If we follow this, the sum of shareholding of Group' Companies in XYZ Company comes to 85% resulting in an NCI of 15%. Accordingly, Auditors is of the view that the only option available with the XYZ Company is to apply "Predecessor Method" of accounting

Opinion:

Paragraph B1 of IFRS 3 describes Business Combinations Under Common Control (BCUCC) as 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. It describes Business Combinations under Common Control as follows:

*"**A business combination involving entities or businesses under common control is a business combination in which all of 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."*

In this case, the transaction meets the definition of common control transaction as the controlling party (Ultimate Parent ABC Foundation) of the XYZ Company remains same before and after the transaction of purchase of business unit by XYZ Company from ABC Foundation.

The Accounting Standard on 'Accounting of Common Control Transactions' notified by SECP, provides for 'method of accounting' in a common control transaction as follows:

"Method of accounting of common control transaction

*[**Refer: Basis of Conclusions paragraphs BC37-BC 60**]*

18. The receiving entity with insignificant non-controlling interest shall account for a common control transaction in its financial statements by applying the 'Predecessor method' as explained in this Accounting Standard.

19. The receiving entity with significant non-controlling interest may elect to apply 'Predecessor method' or 'Acquisition method' to account for a common control transaction in its financial statements.

20. For the purposes of above requirements, non-controlling interest of twenty-five percent or above shall be considered as 'significant'. On the other hand, non-controlling interest of less than twenty-five percent shall be considered as 'insignificant'."

(Bold and Italic ours)

The Key questions arising from the enquiry are discussed and responded as follows:

(a) What is meant by the term 'non-controlling interest' used in paragraph 18 of the Accounting Standard 'Accounting of Common Control Transactions'?

Paragraph 12 of the Accounting Standard 'Accounting of Common Control transactions' (here-in-after referred to as 'the Accounting Standard') states as follows:

"For understanding and application of this Accounting Standard, the terms as defined in the IFRSs shall be used, unless those terms conflict with this Accounting Standard."

It is to be noted Basis of Conclusions Paragraphs BC56-BC58 of the Standard helps us understand the intent of using the term 'non-controlling interest' in paragraphs 18-20 of the Standard.

The relevant Basis of Conclusions paragraphs of the Accounting Standard and explanatory comments thereon are as follows:

*BC55. The Board also considered that the financial information needs of **non-controlling-interest** could be different from the majority shareholders. **Therefore, despite the cost aspect, the significant non-controlling-interest holders should have the ability to obtain relevant information from the entity in the financial statements**. **The management of the receiving entity for the meeting the information needs of significant non-controlling shareholders should be allowed flexibility for adopting an accounting method for common control transactions, which would best serve the information needs of the significant non-controlling shareholders.***

From reading of **above paragraph**, it is clear that the term 'non-controlling-interest holders' and 'non-controlling shareholders' have been used for the same meaning i.e. non-controlling shareholders.

The other relevant paragraphs of the Accounting Standard are BC56, BC57 and BC58, which are reproduced and explained as follows:

*BC56. The Board concluded that **where a receiving entity in a common control transaction has a significant non-controlling interest**, management may elect to apply acquisition method for the common control transaction.*

The above paragraph discusses non-controlling interest in receiving entity and provides Board's conclusion that when such non-controlling interest in receiving entity is significant, management may elect to apply acquisition method for the common control transaction.

Further, this paragraph follows paragraph B55 which discusses the information needs of non-controlling shareholders when they are significant. It means that both paragraph B55 and B56 are interlinked and the intent is to refer and determine information needs of non-controlling shareholders of the receiving Company and are giving management a choice to elect to apply acquisition method for common control transaction when interest of such non-controlling shareholders of the receiving Company is significant.

Paragraph BC57, as reproduced below, is written in continuation to paragraph BC56 and begins with the sentence '***Having concluded on the policy choice in scenario where the receiving entity has significant non-controlling shareholders, the Board decided***……..'

"BC57. Having concluded on the policy choice in scenario where the receiving entity has significant non-controlling shareholders, the Board decided that the mode of selection of the accounting method, including the manner of communication between management and shareholders regarding selection and application of an accounting method is primarily not an accounting matter."

The conclusion made by the Board (as referred to in paragraph B57) is already stated in paragraph B56 which states as follows:

*'BC56. The Board concluded that **where a receiving entity in a common control transaction has a significant non-controlling interest**, management may elect to apply acquisition method for the common control transaction.'*

From reading of both paragraphs B56 and B57 together, it becomes clear that the term 'non-controlling interest' is used to mean shareholding of 'non-controlling shareholders' in the receiving Company.

When we further read **paragraph BC58** (as reproduced below), it becomes clear that the term 'non-controlling-interest' and 'non-controlling shareholding' have been used for the same meaning i.e. shareholding of non-controlling shareholders in the receiving Company.

*BC58. The Board also recognised that the assessment of whether the **non-controlling interest** is significant requires judgement and there can be no accurate quantitative threshold to make this assessment. The term significant and substantive is used in various IFRSs, however, there is no fixed quantitative threshold for determination of significant or substantive. The Board **in context of the determination of significant non-controlling shareholders** noted that in the absence of any quantitative threshold there is risk of diversity in practices. This diverse and divergent understanding and assessment of **significant (and insignificant) non-controlling-shareholding** would lead to divergent accounting of common control transactions of same and similar nature. Therefore, the Board concluded that it should advise a quantitative threshold for assessing **significance of non-controlling interest in a receiving entity** carrying out a common control transaction.*

Based on above, it is clear that the term 'non-controlling shareholders of the receiving entity' and 'non-controlling interest in the receiving Company' have been used inter-changeably in the Basis of Conclusions Paragraphs of the Accounting Standard.

Accordingly, the term 'non-controlling interest' used in paragraphs 18-20 of the Accounting Standard, should be taken to mean direct shareholding of non-controlling shareholders of the receiving entity.

The term 'receiving entity' is defined in paragraph 13 (a) of the Accounting Standard as "*the entity which receives control over one or more entities (or businesses)".*

In the present case, the acquiring Company XYZ Company is receiving entity, and therefore, the shareholding of non-controlling shareholders of XYZ Company only should be considered while determining method of accounting in terms of requirements of paragraphs 18-20 of the Accounting Standard.

(b) Whether 'non-controlling interest' in the receiving Company in the enquired case, is significant in terms of requirements of the Accounting Standard, and which method should be applied for accounting of given common control transaction as per the requirements of the Accounting Standard?

Paragraphs 18 and 20 of the Accounting Standard state as follows:

"18. The receiving entity with insignificant non-controlling interest shall account for a common control transaction in its financial statements by applying the 'Predecessor method' as explained in this Accounting Standard."

"20. For the purposes of above requirements, non-controlling interest of twenty-five percent or above shall be considered as 'significant'. On the other hand, non-controlling interest of less than twenty-five percent shall be considered as 'insignificant'."

In case of XYZ Company (receiving Company), its shareholding structure can be categorized into two main groups:

- **Group Shareholding** which includes ownership interests held by the Ultimate Parent of XYZ Company and its affiliated group companies, collectively representing a single group.

- **Non-Controlling Shareholders of receiving Company** which are minority shareholders who hold direct shareholdings in XYZ Company, independent of the group.

Paragraph 20 of the Accounting Standard prescribes non-controlling interest of twenty-five percent or above as 'significant'.

In this case, the shareholding of non-controlling shareholders of XYZ Company is not significant as it is around 15 percent and does not meet the criteria of 25 percent for considering it as 'significant' non-controlling interest in XYZ Company in terms of requirements of paragraph 20 of the Accounting Standard.

The Board's conclusion

The Board based on the enquired fact pattern, concluded that:

- the term 'non-controlling interest' used in paragraphs 18-20 of the Accounting Standard, is intended to mean 'shareholding of non-controlling shareholders' of the receiving entity.

- In this case, the shareholding of non-controlling shareholders of receiving Company XYZ Company is not significant as it is around 15 percent and does not meet the criteria of 25 percent for considering it as 'significant' non-controlling interest in XYZ Company in terms of requirements of paragraph 20 of the Accounting Standard.

- In view of above, XYZ Company should apply predecessor method of accounting of common control transaction [i.e. acquisition of cereal business unit from its ultimate parent ABC Foundation] in terms of requirements of paragraph 18 & 20 of the Accounting Standard.

(Issued in May 29, 2025)

Disclaimer

The Board believes that the enquired matter, transaction or arrangement has been or will be made considering the legal, ethical and moral requirements. The comments and opinion are based on the facts and circumstances provided by the enquirer. The comments and opinion may change if the facts and the circumstances change. An opinion may also change due to subsequent change in law, pronouncements made by the Institute and other relevant changes. The Institute, its staff and the Board will have no liability in connection with such opinion and this opinion is not a 'legal advice'.