BDO

PBE IFRS 3: BUSINESS COMBINATIONS

Version 1: 2014

Effective Periods Beginning
1 July 2014

IDENTIFYING A BUSINESS COMBINATION / SCOPE

A business combination is:

- A transaction or other event in which acquirer obtains **control** over a **business** (e.g. acquisition of shares or net assets, legal mergers, reverse acquisitions).

PBE IFRS 3 does not apply to:

- The formation of a joint venture.
- Acquisition of an asset or group of assets that is not a business.
- A combination of entities or businesses under common control.
- A business combination arising from a local authority reorganisation.

Definition of "Control"

Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

Definition of a "Business"

- Integrated set of activities and assets;
- Capable of being conducted and managed to provide return or for providing goods or services for community or social benefit.
- Returns include dividends and cost savings.

Acquisition Costs

- CANNOT be capitalised, must instead be expensed in the period they are incurred.
- Professional fees and general administration costs
  - Includes: finders fees, advisory, legal, accounting, valuation and other.

However, costs to issue debt or equity are recognised in accordance with PBE IPSAS 28 - *Financial Instruments: Presentation* and PBE IPSAS 29: Financial Instruments: *Recognition and Measurement*.

ACQUISITION METHOD

A business combination must be accounted for by applying the acquisition method.

STEP 1. IDENTIFY ACQUIRER

PBE IPSAS 6- *Consolidated and Separate Financial Statements* guidance is used to identify the acquirer - the entity that obtains **control** of the acquiree.

STEP 2. DETERMING THE ACQUISITION DATE

The **date** on which the acquirer obtains control of the acquiree.

STEP 3. RECOGNITION AND MEASUREMENT OF IDENTIFIABLE ASSETS, LIABILITIES AND NON-CONTROLLING INTERESTS (NCI)

- As of the acquisition date, the acquirer recognises, separately from goodwill:
  - The identifiable assets acquired;
  - The liabilities assumed (includes contingent liabilities); and
  - Any NCI in the acquiree.
- The acquired assets and liabilities are required to be measured at their **acquisition-date fair values.**
- NCI interests that are present ownership interests and entitle their holders to a proportionate share of the entity's net assets in the event of liquidation (e.g. shares) are measured at acquisition-date fair value or at the NCI's proportionate share in the net assets (accounting policy election).
- All other components of NCI are required to be measured at their acquisition-date fair value.
- There are certain exceptions to the recognition and/or measurement principles which cover contingent liabilities, income taxes, employee benefits, indemnification assets, reacquired rights, share-based payments and assets held for sale.

STEP 4. RECOGNITION AND MEASUREMENT OF GOODWILL OR A GAIN FROM A BARGAIN PURCHASE

- Goodwill is required to be measured as the excess between:
  - The aggregate of the consideration transferred, any non-controlling interest in the acquiree and, in a business combination achieved in stages, the acquisition-date fair value of the acquirer's previously held equity interest in the acquiree; and
  - The net identifiable assets acquired (including any deferred tax balances).
- Goodwill can be grossed up to include the amounts attributable to NCI.
- If the acquirer has made a gain from a **bargain purchase** that gain is recognised in surplus or deficit immediately.
- The consideration transferred in a business combination (including any contingent consideration) is measured at fair value.
- Contingent consideration is either classified as a liability or an equity instrument on the basis of PBE IPSAS 28.
- Contingent consideration that is within the scope of PBE IPSAS 29 (classified as a financial liability) needs to be remeasured to fair value at each reporting date with changes reported in surplus or deficit.

TIER 2 RDR REPORTERS

RDR Reporters are granted certain disclosure exemptions under PBE IFRS 3.

ADDITIONAL GUIDANCE FOR APPLYING THE ACQUISITION METHOD

STEP ACQUISTIONS

- An acquirer sometimes obtains control of an acquiree in which it held an equity interest immediately before the acquisition date. This is known as a business combination achieved in stages or a step acquisition.
- Obtaining control triggers re-measurement of previous investment (equity interests).
- The acquirer remeasured its previously held equity interest in the acquiree at its acquisition-date fair value. Any resulting gain/loss is recognised in surplus or deficit.

BUSINESS COMBINATION WITHOUT TRANSFER OF CONSIDERATION

- The acquisition method of accounting for a business combination also applies if no consideration is transferred.
- Such circumstances include:
  - The acquiree repurchases a sufficient number of its own shares for an existing investor (the acquirer) to obtain control.
  - Minority veto rights lapse that previously kept the acquirer from controlling an acquiree in which the acquirer held the majority voting rights.
  - The acquirer and the acquiree agree to combine their businesses by contract alone.

SUBSEQUENT MEASUREMENT AND ACCOUNTING

- In general, after the date of a business combination, an acquirer measures and accounts for assets acquired and liabilities assumed or incurred in accordance with other applicable PBE Standards.
- However, PBE IFRS 3 includes accounting requirements for reacquired rights, contingent liabilities, contingent consideration and indemnification assets.

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