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Sri Lanka Accounting Standards – SLFRS 03 Business Combination

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SLFRS 03 – Business Combination

A business combination is a transaction or event in which an acquirer obtains control of one or more businesses.

Business combination.

A business combination is a transaction or event in which an acquirer obtains control of one or more businesses. A business is defined as an integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing a return directly to investors or other owners, members or participants.

Scope exclusions.

SLFRS 3 does not apply to the formation of a joint venture, combinations of entities or businesses under common control.

The acquisition method is used for all business combinations.

Steps in applying the acquisition method are:

1. Identification of the 'acquirer' – the combining entity that obtains control of the acquiree

2. Determination of the 'acquisition date' – the date on which the acquirer obtains control of the acquiree

3. Recognition and measurement of the identifiable assets acquired, the liabilities assumed and any non-controlling interest (NCI, formerly called minority interest) in the acquiree

4. Recognition and measurement of goodwill or a gain from a bargain purchase

Measurement of acquired assets and liabilities.

Assets and liabilities are measured at their acquisition-date fair value (with a limited number of specified exceptions).

Measurement of NCI.

SLFRS 3 allows an accounting policy choice, available on a transaction by transaction basis, to measure NCI either at:

- Fair value (sometimes called the full goodwill method), or

- The NCI's proportionate share of net assets of the acquiree (option is available on a transaction by transaction basis).

Example

P pays 800 to purchase 80% of the shares of S. Fair value of 100% of S's identifiable net assets is 600. If P elects to measure non-controlling interests as their proportionate interest in the net assets of S of 120 (20% x 600), the consolidated financial statements show goodwill of 320 (800 +120 - 600).

If P elects to measure non-controlling interests at fair value and determines that fair value to be 185, then goodwill of 385 is recognized (800 + 185 - 600). The fair value of the 20% non-controlling interest in S will not necessarily be proportionate to the price paid by P for its 80%, primarily due to control premium or discount as explained in paragraph B45 of SLFRS 3.

Acquired intangible assets.

Must always be recognized and measured at fair value. There is no 'reliable measurement' exception.

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Goodwill

Goodwill is measured as the difference between:

- the aggregate of (i) the acquisition-date fair value of the consideration transferred, (ii) the amount of any NCI, and (iii) in a business combination achieved in stages (see Below), the acquisition-date fair value of the acquirer's previously-held equity interest in the acquiree; and

- the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed (measured in accordance with SLFRS 3). [SLFRS 3.32]

Example No - 01

Alfa has acquired 80% of Beta on 01st Jan 2016. Statement of Financial position as at 01st Jan 2016. Market value per share as at 01 jan 2016 is Rs 18.

Liabilities	Alfa	Beta	Assets	Alfa	Beta
Share Capital (Rs 10)	200,000	100,000	PPE	100,000	175,000
Reserves	80,000	50,000	Investment in subsidiary	200,000	
Non Current Liabilities	50,000	40,000	**Current assets**		
Current Liabilities			Inventory	20,000	10,000
Trade payable	35,000	20,000	Trade receivable	30,000	20,000
			Cash	15,000	5,000
	365,000	**210,000**		***365,000***	***210,000***

Bargain purchase

If the difference is negative, the resulting gain is recognised as a bargain purchase in profit or loss.

Cost of an Acquisition

Measurement.

Consideration for the acquisition includes the acquisition-date fair value of contingent consideration. Changes to contingent consideration resulting from events after the acquisition date must be recognised in profit or loss

Acquisition cost.

Costs of issuing debt or equity instruments are accounted for under LKAS 32 and LKAS 39. All other costs associated with the acquisition must be expensed, including reimbursements to the acquiree for bearing some of the acquisition costs. Examples of costs to be expensed include finder's fees; advisory, legal, accounting, valuation and other professional or consulting fees; and general administrative costs, including the costs of maintaining an internal acquisitions department.

Contingent consideration.

Contingent consideration must be measured at fair value at the time of the business combination. If the amount of contingent consideration changes as a result of a post-acquisition event (such as meeting an earnings target), accounting for the change in consideration depends on whether the additional consideration is an equity instrument or cash or other assets paid or owed.

If it is equity, the original amount is not remeasured. If the additional consideration is cash or other assets paid or owed, the changed amount is recognised in profit or loss. If the amount of consideration changes because of new information about the fair value of the amount of consideration at acquisition date (rather than because of a post-acquisition event) then retrospective restatement is required.

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Disclosure

- Disclosure of information about current business combinations
- The acquirer shall disclose information that enables users of its financial statements to evaluate the nature and financial effect of a business combination that occurs either during the current reporting period or after the end of the period but before the financial statements are authorised for issue. [SLFRS 3.59]

Disclosure

- name and a description of the acquiree
- acquisition date
- percentage of voting equity interests acquired
- primary reasons for the business combination and a description of how the acquirer obtained control of the acquiree. description of the factors that make up the goodwill recognised

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Disclosure

- qualitative description of the factors that make up the goodwill recognised, such as expected synergies from combining operations, intangible assets that do not qualify for separate recognition
- acquisition-date fair value of the total consideration transferred and the acquisition-date fair value of each major class of consideration
- details of contingent consideration arrangements and indemnification assets

Disclosure

- details of acquired receivables
- the amounts recognised as of the acquisition date for each major class of assets acquired and liabilities assumed
- details of contingent liabilities recognised
- total amount of goodwill that is expected to be deductible for tax purposes
- details of any transactions that are recognised separately from the acquisition of assets and assumption of liabilities in the business combination

Disclosure

- information about a bargain purchase ('negative goodwill')
- for each business combination in which the acquirer holds less than 100 per cent of the equity interests in the acquiree at the acquisition date, various disclosures are required
- details about a business combination achieved in stages
- information about the acquiree's revenue and profit or loss
- information about a business combination whose acquisition date is after the end of the reporting period but before the financial statements are authorised for issue

Thank you.