

International Financial Reporting Standard 3

Business Combinations

This version was issued in January 2008. Its effective date is 1 July 2009.

IAS 22 *Business Combinations* was issued by the International Accounting Standards Committee in October 1998. It was a revision of IAS 22 *Business Combinations* (issued in December 1993), which replaced IAS 22 *Accounting for Business Combinations* (issued in November 1983).

In April 2001 the International Accounting Standards Board (IASB) resolved that all Standards and Interpretations issued under previous Constitutions continued to be applicable unless and until they were amended or withdrawn.

In March 2004 the IASB issued IFRS 3 *Business Combinations*. It replaced IAS 22 and three Interpretations:

- SIC-9 *Business Combinations—Classification either as Acquisitions or Unitings of Interests*
- SIC-22 *Business Combinations—Subsequent Adjustment of Fair Values and Goodwill Initially Reported*
- SIC-28 *Business Combinations—“Date of Exchange” and Fair Value of Equity Instruments*.

IFRS 3 was amended by IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* (issued March 2004).

IAS 1 *Presentation of Financial Statements* (as revised in September 2007)* amended the terminology used throughout IFRSs, including IFRS 3.

In January 2008 the IASB issued a revised IFRS 3.

The following Interpretations refer to IFRS 3:

- SIC-32 *Intangible Assets—Web Site Costs* (issued March 2002 and amended by IFRS 3 in March 2004)
- IFRIC 9 *Reassessment of Embedded Derivatives* (issued March 2006)
- IFRIC 17 *Distributions of Non-cash Assets to Owners* (issued November 2008).†

* effective date 1 January 2009

† effective date 1 July 2009

CONTENTS

paragraphs

INTRODUCTION	IN1–IN13
INTERNATIONAL FINANCIAL REPORTING STANDARD 3 BUSINESS COMBINATIONS	
OBJECTIVE	1
SCOPE	2
IDENTIFYING A BUSINESS COMBINATION	3
THE ACQUISITION METHOD	4–53
Identifying the acquirer	6–7
Determining the acquisition date	8–9
Recognising and measuring the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree	10–31
Recognition principle	10–17
Recognition conditions	11–14
Classifying or designating identifiable assets acquired and liabilities assumed in a business combination	15–17
Measurement principle	18–20
Exceptions to the recognition or measurement principles	21–31
Exception to the recognition principle	22–23
Contingent liabilities	22–23
Exceptions to both the recognition and measurement principles	24–28
Income taxes	24–25
Employee benefits	26
Indemnification assets	27–28
Exceptions to the measurement principle	29–31
Reacquired rights	29
Share-based payment awards	30
Assets held for sale	31
Recognising and measuring goodwill or a gain from a bargain purchase	32–40
Bargain purchases	34–36
Consideration transferred	37–40
Contingent consideration	39–40
Additional guidance for applying the acquisition method to particular types of business combinations	41–44
A business combination achieved in stages	41–42
A business combination achieved without the transfer of consideration	43–44
Measurement period	45–50
Determining what is part of the business combination transaction	51–53
Acquisition-related costs	53
SUBSEQUENT MEASUREMENT AND ACCOUNTING	54–58
Reacquired rights	55

Contingent liabilities	56
Indemnification assets	57
Contingent consideration	58
DISCLOSURES	59–63
EFFECTIVE DATE AND TRANSITION	64–67
Effective date	64
Transition	65–67
Income taxes	67
WITHDRAWAL OF IFRS 3 (2004)	68
APPENDICES:	
A Defined terms	
B Application guidance	
C Amendments to other IFRSs	
APPROVAL BY THE BOARD OF IFRS 3 ISSUED IN JANUARY 2008	
BASIS FOR CONCLUSIONS	
DISSENTING OPINIONS	
APPENDIX	
Amendments to the Basis for Conclusions on other IFRSs	
ILLUSTRATIVE EXAMPLES	
APPENDIX	
Amendments to guidance on other IFRSs	
COMPARISON OF IFRS 3 AND SFAS 141(R)	
TABLE OF CONCORDANCE	

IFRS 3

International Financial Reporting Standard 3 *Business Combinations* (IFRS 3) is set out in paragraphs 1–68 and Appendices A–C. All the paragraphs have equal authority. Paragraphs in **bold type** state the main principles. Terms defined in Appendix A are in *italics* the first time they appear in the IFRS. Definitions of other terms are given in the Glossary for International Financial Reporting Standards. IFRS 3 should be read in the context of its objective and the Basis for Conclusions, the *Preface to International Financial Reporting Standards* and the *Framework for the Preparation and Presentation of Financial Statements*. IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

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Introduction

Reasons for issuing the IFRS

- IN1 The revised International Financial Reporting Standard 3 *Business Combinations* (IFRS 3) is part of a joint effort by the International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB) to improve financial reporting while promoting the international convergence of accounting standards. Each board decided to address the accounting for business combinations in two phases. The IASB and the FASB deliberated the first phase separately. The FASB concluded its first phase in June 2001 by issuing FASB Statement No. 141 *Business Combinations*. The IASB concluded its first phase in March 2004 by issuing the previous version of IFRS 3 *Business Combinations*. The boards' primary conclusion in the first phase was that virtually all business combinations are acquisitions. Accordingly, the boards decided to require the use of one method of accounting for business combinations—the acquisition method.
- IN2 The second phase of the project addressed the guidance for applying the acquisition method. The boards decided that a significant improvement could be made to financial reporting if they had similar standards for accounting for business combinations. Thus, they decided to conduct the second phase of the project as a joint effort with the objective of reaching the same conclusions. The boards concluded the second phase of the project by issuing this IFRS and FASB Statement No. 141 (revised 2007) *Business Combinations* and the related amendments to IAS 27 *Consolidated and Separate Financial Statements* and FASB Statement No. 160 *Noncontrolling Interests in Consolidated Financial Statements*.
- IN3 The IFRS replaces IFRS 3 (as issued in 2004) and comes into effect for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009. Earlier application is permitted, provided that IAS 27 (as amended in 2008) is applied at the same time.

Main features of the IFRS

- IN4 The objective of the IFRS is to enhance the relevance, reliability and comparability of the information that an entity provides in its financial statements about a business combination and its effects. It does that by establishing principles and requirements for how an acquirer:
- (a) recognises and measures in its financial statements the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree;
 - (b) recognises and measures the goodwill acquired in the business combination or a gain from a bargain purchase; and
 - (c) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination.

Core principle

- IN5 An acquirer of a business recognises the assets acquired and liabilities assumed at their acquisition-date fair values and discloses information that enables users to evaluate the nature and financial effects of the acquisition.

Applying the acquisition method

- IN6 A business combination must be accounted for by applying the acquisition method, unless it is a combination involving entities or businesses under common control. One of the parties to a business combination can always be identified as the acquirer, being the entity that obtains control of the other business (the acquiree). Formations of a joint venture or the acquisition of an asset or a group of assets that does not constitute a business are not business combinations.
- IN7 The IFRS establishes principles for recognising and measuring the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. Any classifications or designations made in recognising these items must be made in accordance with the contractual terms, economic conditions, acquirer's operating or accounting policies and other factors that exist at the acquisition date.
- IN8 Each identifiable asset and liability is measured at its acquisition-date fair value. Any non-controlling interest in an acquiree is measured at fair value or as the non-controlling interest's proportionate share of the acquiree's net identifiable assets.
- IN9 The IFRS provides limited exceptions to these recognition and measurement principles:
- (a) Leases and insurance contracts are required to be classified on the basis of the contractual terms and other factors at the inception of the contract (or when the terms have changed) rather than on the basis of the factors that exist at the acquisition date.
 - (b) Only those contingent liabilities assumed in a business combination that are a present obligation and can be measured reliably are recognised.
 - (c) Some assets and liabilities are required to be recognised or measured in accordance with other IFRSs, rather than at fair value. The assets and liabilities affected are those falling within the scope of IAS 12 *Income Taxes*, IAS 19 *Employee Benefits*, IFRS 2 *Share-based Payment* and IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*.
 - (d) There are special requirements for measuring a reacquired right.
 - (e) Indemnification assets are recognised and measured on a basis that is consistent with the item that is subject to the indemnification, even if that measure is not fair value.

- IN10 The IFRS requires the acquirer, having recognised the identifiable assets, the liabilities and any non-controlling interests, to identify any difference between:
- (a) 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
 - (b) the net identifiable assets acquired.

The difference will, generally, be recognised as goodwill. If the acquirer has made a gain from a bargain purchase that gain is recognised in profit or loss.

- IN11 The consideration transferred in a business combination (including any contingent consideration) is measured at fair value.
- IN12 In general, an acquirer measures and accounts for assets acquired and liabilities assumed or incurred in a business combination after the business combination has been completed in accordance with other applicable IFRSs. However, the IFRS provides accounting requirements for reacquired rights, contingent liabilities, contingent consideration and indemnification assets.

Disclosure

- IN13 The IFRS requires the acquirer to disclose information that enables users of its financial statements to evaluate the nature and financial effect of business combinations that occurred during the current reporting period or after the reporting date but before the financial statements are authorised for issue. After a business combination, the acquirer must disclose any adjustments recognised in the current reporting period that relate to business combinations that occurred in the current or previous reporting periods.

International Financial Reporting Standard 3 **Business Combinations**

Objective

- 1 The objective of this IFRS is to improve the relevance, reliability and comparability of the information that a reporting entity provides in its financial statement about a *business combination* and its effects. To accomplish that, this IFRS establishes principles and requirements for how the *acquirer*:
- (a) recognises and measures in its financial statements the *identifiable* assets acquired, the liabilities assumed and any *non-controlling interest* in the *acquiree*;
 - (b) recognises and measures the *goodwill* acquired in the business combination or a gain from a bargain purchase; and
 - (c) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination.

Scope

- 2 This IFRS applies to a transaction or other event that meets the definition of a business combination. This IFRS does not apply to:
- (a) the formation of a joint venture.
 - (b) the acquisition of an asset or a group of assets that does not constitute a *business*. In such cases the acquirer shall identify and recognise the individual identifiable assets acquired (including those assets that meet the definition of, and recognition criteria for, *intangible assets* in IAS 38 *Intangible Assets*) and liabilities assumed. The cost of the group shall be allocated to the individual identifiable assets and liabilities on the basis of their relative *fair values* at the date of purchase. Such a transaction or event does not give rise to goodwill.
 - (c) a combination of entities or businesses under common control (paragraphs B1–B4 provide related application guidance).

Identifying a business combination

- 3 An entity shall determine whether a transaction or other event is a business combination by applying the definition in this IFRS, which requires that the assets acquired and liabilities assumed constitute a business. If the assets acquired are not a business, the reporting entity shall account for the transaction or other event as an asset acquisition. Paragraphs B5–B12 provide guidance on identifying a business combination and the definition of a business.

The acquisition method

- 4 **An entity shall account for each business combination by applying the acquisition method.**
- 5 Applying the acquisition method requires:
- (a) identifying the acquirer;
 - (b) determining the *acquisition date*;
 - (c) recognising and measuring the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree; and
 - (d) recognising and measuring goodwill or a gain from a bargain purchase.

Identifying the acquirer

- 6 **For each business combination, one of the combining entities shall be identified as the acquirer.**
- 7 The guidance in IAS 27 *Consolidated and Separate Financial Statements* shall be used to identify the acquirer—the entity that obtains *control* of the acquiree. If a business combination has occurred but applying the guidance in IAS 27 does not clearly indicate which of the combining entities is the acquirer, the factors in paragraphs B14–B18 shall be considered in making that determination.

Determining the acquisition date

- 8 **The acquirer shall identify the acquisition date, which is the date on which it obtains control of the acquiree.**
- 9 The date on which the acquirer obtains control of the acquiree is generally the date on which the acquirer legally transfers the consideration, acquires the assets and assumes the liabilities of the acquiree—the closing date. However, the acquirer might obtain control on a date that is either earlier or later than the closing date. For example, the acquisition date precedes the closing date if a written agreement provides that the acquirer obtains control of the acquiree on a date before the closing date. An acquirer shall consider all pertinent facts and circumstances in identifying the acquisition date.

Recognising and measuring the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree

Recognition principle

- 10 **As of the acquisition date, the acquirer shall recognise, separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. Recognition of identifiable assets acquired and liabilities assumed is subject to the conditions specified in paragraphs 11 and 12.**

Recognition conditions

- 11 To qualify for recognition as part of applying the acquisition method, the identifiable assets acquired and liabilities assumed must meet the definitions of assets and liabilities in the *Framework for the Preparation and Presentation of Financial Statements* at the acquisition date. For example, costs the acquirer expects but is not obliged to incur in the future to effect its plan to exit an activity of an acquiree or to terminate the employment of or relocate an acquiree's employees are not liabilities at the acquisition date. Therefore, the acquirer does not recognise those costs as part of applying the acquisition method. Instead, the acquirer recognises those costs in its post-combination financial statements in accordance with other IFRSs.
- 12 In addition, to qualify for recognition as part of applying the acquisition method, the identifiable assets acquired and liabilities assumed must be part of what the acquirer and the acquiree (or its former *owners*) exchanged in the business combination transaction rather than the result of separate transactions. The acquirer shall apply the guidance in paragraphs 51–53 to determine which assets acquired or liabilities assumed are part of the exchange for the acquiree and which, if any, are the result of separate transactions to be accounted for in accordance with their nature and the applicable IFRSs.
- 13 The acquirer's application of the recognition principle and conditions may result in recognising some assets and liabilities that the acquiree had not previously recognised as assets and liabilities in its financial statements. For example, the acquirer recognises the acquired identifiable intangible assets, such as a brand name, a patent or a customer relationship, that the acquiree did not recognise as assets in its financial statements because it developed them internally and charged the related costs to expense.
- 14 Paragraphs B28–B40 provide guidance on recognising operating leases and intangible assets. Paragraphs 22–28 specify the types of identifiable assets and liabilities that include items for which this IFRS provides limited exceptions to the recognition principle and conditions.

Classifying or designating identifiable assets acquired and liabilities assumed in a business combination

- 15 **At the acquisition date, the acquirer shall classify or designate the identifiable assets acquired and liabilities assumed as necessary to apply other IFRSs subsequently. The acquirer shall make those classifications or designations on the basis of the contractual terms, economic conditions, its operating or accounting policies and other pertinent conditions as they exist at the acquisition date.**
- 16 In some situations, IFRSs provide for different accounting depending on how an entity classifies or designates a particular asset or liability. Examples of classifications or designations that the acquirer shall make on the basis of the pertinent conditions as they exist at the acquisition date include but are not limited to:
- (a) classification of particular financial assets and liabilities as a financial asset or liability at fair value through profit or loss, or as a financial asset available for sale or held to maturity, in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*;