SLFRS 03 – BUSINESS COMBINATION

- A **business combination** is a transaction or event in which an acquirer obtains control of one or more businesses. EX. True mergers
- Examples- Methods Used to obtain control
- Transfer of cash, cash equivalents or other assets
- Incurring liabilities
- Issuing equity interests
- Providing more than one type of consideration
- by contract alone.

- Example of Structures
- Acquisition of Subsidiaries
- Transfer of Net asset
- Merge of the acquired business into the acquirer's operations ☐

WHAT IS A BUSINESS

- 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 in the form of dividends
- Lower cost or
- Other economic benefits
- directly to investors or other owners, members or participants.

SCOPE EXCLUSIONS.

- SLFRS 3 does not apply to the formation of a joint venture (LKAS 31)
- combinations of entities or businesses under common control. Common Control- A business combination in which all of the combining entities or businesses are ultimately controlled by the same parties before and after the combination

ACCOUNTING FOR BUSINESS COMBINATIONS

- 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 noncontrolling interest (NCI, for merly called minority interest) in the acquiree
- 4. Recognition and measurement of goodwill or a gain from a bargain purchase

IDENTIFYING THE ACQUIRER

- The entity that obtains control of the other entities business . To obtain the control , entity pays the consideration as cash and exchanging equity
- **How to obtain the control**
- Power over one half of the voting rights-ownership or contract
- Power to govern the financial and operating policies via statute or agreement
- Power to appoint or remove the majority of the members of the board or body that controls the entity.
- Power to cast the majority of votes at meetings of the board or body that controls the entity
- Existence of potential voting rights that are currently exercisable or convertible.

MEASUREMENT OF ACQUIRED ASSETS AND LIABILITIES.

- Assets and liabilities are measured at fair value on their acquisition-date .
- Fair value – the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participant at the measurement date.
- Non contoring interest – the equity in a acquiree not attributable directly or indirectly to a acquirer

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 has payed 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),
- If P elects to measure non-controlling interests at fair value and determines that fair value to be 185,

MEASURING GOODWILL

- The acquirer should recognize goodwill at the acquisition date , measured as the excess of ;
- The aggregate of Consideration transferred generally measured at fair value
- The amount of any NCI in the acquire (the two measurement choices under SLRS 03)
- In business combination achieved in any stages, the acquisition date fair value of the acquirer's previously held equity interest in the entity.
- Less; the net of the acquisition date of the amounts of the identifiable asstes acquired and the liabilities assumed measured in accordance with SLFRS 03

• Fair value of consideration transferred	X
• Add; non controlling interest in entity acquired	X
(alternative measures)	
Add ; acquisition date fair value of existing holdings in acqiree	X
	X
Less; net identifiable assets acquired	(X)
Goodwill	X

BARGAIN PURCHASE

- A bargain purchase is a business combination in which the net fair value of the identifiable assets acquired exceed the aggregate of ;
- Consideration transferred plus
- Non controlling interest plus
- Fair value of any previously held equity interest in the acquire
- According to SLFRS 03, if there is a bargain purchase the acquirer recognizes the resulting gain in profit or loss on the acquisition date.
- Gain is attributed to the acquirer

EXAMPLE WITH DEFERRED CONSIDERATIONS

- Deferred consideration should be discounted to its present value.
- EX; Date of acquisition is 1 January 2021
- Consideration of 4.2 m paid to be in instalments of 2.1m on 1 January 2021and 2.1 m on 1 January 2023
- Acquirer's incremental borrowing rate is 5%

	cash	factor	PV
1/1/21	(2100)	1.000	(2100)
1/1/23	(2100)	0.9070	(1905)
Total	(4200)		(4005)

- Initially measure consideration at 4005 and record a financial liability as 195 will be expensed as finance cost at an effective rate of interest 5%.

CONTINGENT CONSIDERATION

- Consideration transferred by the acquirer , including contingent consideration must be measured and recognized at fair value at the acquisition date .
- Ex;Acquirer paid 5400 to acquire S Ltd.
  Fair value of the net assets of S Ltd is 3800
- Acquirer also agrees to pay 5% of revenue for all business that is referred by the seller of S Ltd.Within three years.
- The budget of S Ltd.Anticipates total referred income of 17500 over the three years period.

- Initial Reignition ; Calculation of the PV of contingent consideration is
- 17500* 5%= 875
- Goodwill is ,

Consideration	5400
Contingent consideration	875
	6275
Fair value of NA	(3800)
Goodwill	2475

ACQUISITION COST

- Acquisition cost that are not part of the consideration transferred.
- Acquirer may incur cost in addition to the consideration transferred that are associated with the acquisition.
- Ex. Finder's fees, advisory , legal , accounting, valuation , and other professional or consulting fees , etc.
- They must be expensed as period cost.

STEP ACQUISITION

- In a business combination achieved in stages. The acquirer shall;
- Remeasure his previously held equity interest in the acquiree at its acquisition date fair value.
- Recognize the resulting gain or loss, if any in profit or loss
- What does this mean;
- Possible to generate profit by obtaining control of an entity previously held as an investment or an associate.

EXAMPLE

- Original 30% holding purchased in 2014
- Additional 50% purchased in 2021
- Equity accounted carrying value of original 30% holdings 4.9 m
- Cash consideration 11M
- Fair value of the 100% of net assets 18.7 m
- Fair value of original 30% holding 6.3m

- At the date that control passes , there is a difference between ; the carrying value of investment in the associate (4.9) and the fair value of the investment in the associate
- (6.3). Take the difference of 1.4m to the income statement.
- Acquisition date fair value of original holdings 6.3
- Cash paid for additional holding 11
- 17.3
- Fair value of the net assets acquired 18.7*(30%+50%) (15m)
- Goodwill 2.3m

Or Acquisition date fair value of original holdings	6.3
Cash paid for additional holding	11
NCI (18.7*20%)	3,7
Total value	21
Fair value of the net assets acquired	18.7
Goodwill	2.3m

- In 2021 the remaining 20% is purchased
- Consideration 4.1m
- Fair value of net assets 18. 7m
- No profit or additional goodwill with the acquisition of additional holdings in a control entity.
- Difference between consideration and NIC is accounted for in equity.

- NCI dr. 3.7 (18.7*20%)
- Equity dr. 0.4
- Cash cr. 4.1
- In 2022 55% of holdings are disposed.
- Consideration 12.5m
- Net assets 20.8 M

- Loss of control
- Associate is recognized at fair value.
- Carrying value of associate (12,5*45%/55%) Dr. 10.2M
- Cash Dr. 12.5M
- Net assets Cr. 20.8
- P&L Cr. 1.9