
AMENDMENTS TO STATUTORY BOARD FINANCIAL REPORTING STANDARDS

Definition of a Business

(Amendments to SB-FRS 103)

The amendments apply for annual reporting periods beginning on or after 1 January 2020.
Earlier application is permitted.

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Introduction

This document sets out amendments made to SB-FRS 103 *Business Combinations*.

The amendments clarify the definition of a business, with the objective of assisting entities to determine whether a transaction should be accounted for as a business combination or as an asset acquisition. The amendments:

- (a) clarify that to be considered a business, an acquired set of activities and assets must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create outputs;
- (b) remove the assessment of whether market participants are capable of replacing any missing inputs or processes and continuing to produce outputs;
- (c) add guidance and illustrative examples to help entities assess whether a substantive process has been acquired;
- (d) narrow the definitions of a business and of outputs by focusing on goods and services provided to customers and by removing the reference to an ability to reduce costs; and
- (e) add an optional concentration test that permits a simplified assessment of whether an acquired set of activities and assets is not a business.

Entities are required to apply the amendments to transactions for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 January 2020. Earlier application is permitted.

Amendments to SB-FRS 103 *Business Combinations*

Paragraph 3, the definition of the term 'business' in Appendix A and paragraphs B7–B9, B11 and B12 are amended. Paragraphs 64P, B7A–B7C, B8A and B12A–B12D, and headings above paragraphs B7A, B8 and B12, are added. Paragraph B10 is deleted. New text is underlined and deleted text is struck through.

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 SB-FRS, 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~~B12D provide guidance on identifying a business combination and the definition of a business.

Effective date and transition

Effective date

...

- 64P *Definition of a Business*, issued in March 2019, added paragraphs B7A–B7C, B8A and B12A–B12D, amended the definition of the term 'business' in Appendix A, amended paragraphs 3, B7–B9, B11 and B12 and deleted paragraph B10. An entity shall apply these amendments to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 January 2020 and to asset acquisitions that occur on or after the beginning of that period. Earlier application of these amendments is permitted. If an entity applies these amendments for an earlier period, it shall disclose that fact.

Appendix A

Defined terms

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- business** An integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing goods or services to customers, generating investment income (such as dividends or interest) or generating other income from ordinary activities ~~a return in the form of dividends, lower costs or other economic benefits directly to investors or other owners, members or participants.~~

Definition of a business (application of paragraph 3)

- B7 A business consists of inputs and processes applied to those inputs that have the ability to create contribute to the creation of outputs. Although businesses usually have outputs, outputs are not required for an integrated set to qualify as a business. The three elements of a business are defined as follows (see paragraphs B8–B12D for guidance on the elements of a business):
- (a) **Input:** Any economic resource that creates outputs, or has the ability to create, contribute to the creation of outputs, when one or more processes are applied to it. Examples include non-current assets (including intangible assets or rights to use non-current assets), intellectual property, the ability to obtain access to necessary materials or rights and employees.
 - (b) **Process:** Any system, standard, protocol, convention or rule that, when applied to an input or inputs, creates outputs or has the ability to create contribute to the creation of outputs. Examples include strategic management processes, operational processes and resource management processes. These processes typically are documented, but the intellectual capacity of an organised workforce having the necessary skills and experience following rules and conventions may provide the necessary processes that are capable of being applied to inputs to create outputs. (Accounting, billing, payroll and other administrative systems typically are not processes used to create outputs.)
 - (c) **Output:** The result of inputs and processes applied to those inputs that provide ~~or have the ability to provide a return in the form of dividends, lower costs or other economic benefits directly to investors or other owners, members or participants~~ goods or services to customers, generate investment income (such as dividends or interest) or generate other income from ordinary activities.

Optional test to identify concentration of fair value

- B7A Paragraph B7B sets out an optional test (the concentration test) to permit a simplified assessment of whether an acquired set of activities and assets is not a business. An entity may elect to apply, or not apply, the test. An entity may make such an election separately for each transaction or other event. The concentration test has the following consequences:
- (a) if the concentration test is met, the set of activities and assets is determined not to be a business and no further assessment is needed.
 - (b) if the concentration test is not met, or if the entity elects not to apply the test, the entity shall then perform the assessment set out in paragraphs B8–B12D.
- B7B The concentration test is met if substantially all of the fair value of the gross assets acquired is concentrated in a single identifiable asset or group of similar identifiable assets. For the concentration test:
- (a) gross assets acquired shall exclude cash and cash equivalents, deferred tax assets, and goodwill resulting from the effects of deferred tax liabilities.
 - (b) the fair value of the gross assets acquired shall include any consideration transferred (plus the fair value of any non-controlling interest and the fair value of any previously held interest) in excess of the fair value of net identifiable assets acquired. The fair value of the gross assets acquired may normally be determined as the total obtained by adding the fair value of the consideration transferred (plus the fair value of any non-controlling interest and the fair value of any previously held interest) to the fair value of the liabilities assumed (other than deferred tax liabilities), and then excluding the items identified in subparagraph (a). However, if the fair value of the gross assets acquired is more than that total, a more precise calculation may sometimes be needed.

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- (c) a single identifiable asset shall include any asset or group of assets that would be recognised and measured as a single identifiable asset in a business combination.
- (d) if a tangible asset is attached to, and cannot be physically removed and used separately from, another tangible asset (or from an underlying asset subject to a lease, as defined in SB-FRS 116 *Leases*), without incurring significant cost, or significant diminution in utility or fair value to either asset (for example, land and buildings), those assets shall be considered a single identifiable asset.
- (e) when assessing whether assets are similar, an entity shall consider the nature of each single identifiable asset and the risks associated with managing and creating outputs from the assets (that is, the risk characteristics).
- (f) the following shall not be considered similar assets:
 - (i) a tangible asset and an intangible asset;
 - (ii) tangible assets in different classes (for example, inventory, manufacturing equipment and automobiles) unless they are considered a single identifiable asset in accordance with the criterion in subparagraph (d);
 - (iii) identifiable intangible assets in different classes (for example, brand names, licences and intangible assets under development);
 - (iv) a financial asset and a non-financial asset;
 - (v) financial assets in different classes (for example, accounts receivable and investments in equity instruments); and
 - (vi) identifiable assets that are within the same class of asset but have significantly different risk characteristics.

B7C The requirements in paragraph B7B do not modify the guidance on similar assets in SB-FRS 38 *Intangible Assets*; nor do they modify the meaning of the term 'class' in SB-FRS 16 *Property, Plant and Equipment*, SB-FRS 38 and SB-FRS 107 *Financial Instruments: Disclosures*.

Elements of a business

- B8 Although businesses usually have outputs, outputs are not required for an integrated set of activities and assets to qualify as a business. To be capable of being conducted and managed for the purposes defined purpose identified in the definition of a business, an integrated set of activities and assets requires two essential elements—inputs and processes applied to those inputs, which together are or will be used to create outputs. However, a A business need not include all of the inputs or processes that the seller used in operating that business if market participants are capable of acquiring the business and continuing to produce outputs, for example, by integrating the business with their own inputs and processes. However, to be considered a business, an integrated set of activities and assets must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output. Paragraphs B12–B12D specify how to assess whether a process is substantive.
- B8A If an acquired set of activities and assets has outputs, continuation of revenue does not on its own indicate that both an input and a substantive process have been acquired.
- B9 The nature of the elements of a business varies by industry and by the structure of an entity's operations (activities), including the entity's stage of development. Established businesses often have many different types of inputs, processes and outputs, whereas new businesses often have few inputs and processes and sometimes only a single output (product). Nearly all businesses also have liabilities, but a business need not have liabilities. Furthermore, an acquired set of activities and assets that is not a business might have liabilities.

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~~B10 An integrated set of activities and assets in the development stage might not have outputs. If not, the acquirer should consider other factors to determine whether the set is a business. Those factors include, but are not limited to, whether the set:~~

- ~~(a) has begun planned principal activities;~~
- ~~(b) has employees, intellectual property and other inputs and processes that could be applied to those inputs;~~
- ~~(c) is pursuing a plan to produce outputs; and~~
- ~~(d) will be able to obtain access to customers that will purchase the outputs.~~

~~Not all of those factors need to be present for a particular integrated set of activities and assets in the development stage to qualify as a business. [Deleted]~~

B11 Determining whether a particular set of activities and assets and ~~activities~~ is a business ~~should~~ shall be based on whether the integrated set is capable of being conducted and managed as a business by a market participant. Thus, in evaluating whether a particular set is a business, it is not relevant whether a seller operated the set as a business or whether the acquirer intends to operate the set as a business.

Assessing whether an acquired process is substantive

~~B12 In the absence of evidence to the contrary, a particular set of assets and activities in which goodwill is present shall be presumed to be a business. However, a business need not have goodwill. Paragraphs B12A–B12D explain how to assess whether an acquired process is substantive if the acquired set of activities and assets does not have outputs (paragraph B12B) and if it does have outputs (paragraph B12C).~~

B12A An example of an acquired set of activities and assets that does not have outputs at the acquisition date is an early-stage entity that has not started generating revenue. Moreover, if an acquired set of activities and assets was generating revenue at the acquisition date, it is considered to have outputs at that date, even if subsequently it will no longer generate revenue from external customers, for example because it will be integrated by the acquirer.

B12B If a set of activities and assets does not have outputs at the acquisition date, an acquired process (or group of processes) shall be considered substantive only if:

- (a) it is critical to the ability to develop or convert an acquired input or inputs into outputs; and
- (b) the inputs acquired include both an organised workforce that has the necessary skills, knowledge, or experience to perform that process (or group of processes) and other inputs that the organised workforce could develop or convert into outputs. Those other inputs could include:
 - (i) intellectual property that could be used to develop a good or service;
 - (ii) other economic resources that could be developed to create outputs; or
 - (iii) rights to obtain access to necessary materials or rights that enable the creation of future outputs.

Examples of the inputs mentioned in subparagraphs (b)(i)–(iii) include technology, in-process research and development projects, real estate and mineral interests.

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B12C If a set of activities and assets has outputs at the acquisition date, an acquired process (or group of processes) shall be considered substantive if, when applied to an acquired input or inputs, it:

- (a) is critical to the ability to continue producing outputs, and the inputs acquired include an organised workforce with the necessary skills, knowledge, or experience to perform that process (or group of processes); or
- (b) significantly contributes to the ability to continue producing outputs and:
 - (i) is considered unique or scarce; or
 - (ii) cannot be replaced without significant cost, effort, or delay in the ability to continue producing outputs.

B12D The following additional discussion supports both paragraphs B12B and B12C:

- (a) an acquired contract is an input and not a substantive process. Nevertheless, an acquired contract, for example, a contract for outsourced property management or outsourced asset management, may give access to an organised workforce. An entity shall assess whether an organised workforce accessed through such a contract performs a substantive process that the entity controls, and thus has acquired. Factors to be considered in making that assessment include the duration of the contract and its renewal terms.
- (b) difficulties in replacing an acquired organised workforce may indicate that the acquired organised workforce performs a process that is critical to the ability to create outputs.
- (c) a process (or group of processes) is not critical if, for example, it is ancillary or minor within the context of all the processes required to create outputs.

Amendments to the Illustrative Examples accompanying SB-FRS 103 *Business Combinations*

Paragraphs IE73–IE123 and their related headings are added.

Definition of a business

IE73 The examples in paragraphs IE74–IE123 illustrate application of the guidance in paragraphs B7–B12D on the definition of a business.

Example A—acquisition of real estate

Scenario 1—Background

IE74 An entity (Purchaser) purchases a portfolio of 10 single-family homes that each have an in-place lease. The fair value of the consideration paid is equal to the aggregate fair value of the 10 single-family homes acquired. Each single-family home includes the land, building and property improvements. Each home has a different floor area and interior design. The 10 single-family homes are located in the same area and the classes of customers (eg tenants) are similar. The risks associated with operating in the real estate market of the homes acquired are not significantly different. No employees, other assets, processes or other activities are transferred.

Scenario 1—Application of requirements

IE75 Purchaser elects to apply the optional concentration test set out in paragraph B7B and concludes that:

- (a) each single-family home is considered a single identifiable asset in accordance with paragraph B7B for the following reasons:
 - (i) the building and property improvements are attached to the land and cannot be removed without incurring significant cost; and
 - (ii) the building and the in-place lease are considered a single identifiable asset, because they would be recognised and measured as a single identifiable asset in a business combination (see paragraph B42).
- (b) the group of 10 single-family homes is a group of similar identifiable assets because the assets (all single-family homes) are similar in nature and the risks associated with managing and creating outputs are not significantly different. This is because the types of homes and classes of customers are not significantly different.
- (c) consequently, substantially all of the fair value of the gross assets acquired is concentrated in a group of similar identifiable assets.

IE76 Therefore, Purchaser concludes that the acquired set of activities and assets is not a business.

Scenario 2—Background

IE77 Assume the same facts as in Scenario 1 except that Purchaser also purchases a multi-tenant corporate office park with six 10-storey office buildings that are fully leased. The additional set of activities and assets acquired includes the land, buildings, leases and contracts for outsourced cleaning, security and maintenance. No employees, other assets, other processes or other activities are transferred. The aggregate fair value associated with the office park is

similar to the aggregate fair value associated with the 10 single-family homes. The processes performed through the contracts for outsourced cleaning and security are ancillary or minor within the context of all the processes required to create outputs.

Scenario 2—Application of requirements

- IE78 Purchaser elects to apply the optional concentration test set out in paragraph B7B and concludes that the single-family homes and the office park are not similar identifiable assets, because the single-family homes and the office park differ significantly in the risks associated with operating the assets, obtaining tenants and managing tenants. In particular, the scale of operations and risks associated with the two classes of customers are significantly different. Consequently, the fair value of the gross assets acquired is not substantially all concentrated in a group of similar identifiable assets, because the fair value of the office park is similar to the aggregate fair value of the 10 single-family homes. Thus Purchaser assesses whether the set meets the minimum requirements to be considered a business in accordance with paragraphs B8–B12D.
- IE79 The set of activities and assets has outputs because it generates revenue through the in-place leases. Consequently, Purchaser applies the criteria in paragraph B12C to determine whether any processes acquired are substantive.
- IE80 Purchaser concludes that the criterion in paragraph B12C(a) is not met because:
- (a) the set does not include an organised workforce; and
 - (b) Purchaser considers that the processes performed by the outsourced cleaning, security and maintenance personnel (the only processes acquired) are ancillary or minor within the context of all the processes required to create outputs (see paragraph B12D(c)) and, therefore, are not critical to the ability to continue producing outputs.
- IE81 After considering the only processes acquired, those performed by the outsourced cleaning, security and maintenance personnel, Purchaser also concludes that the criteria in paragraph B12C(b) are not met. Either of the following reasons justifies that conclusion:
- (a) the processes do not significantly contribute to the ability to continue producing outputs.
 - (b) the processes are readily accessible in the marketplace. Thus, they are not unique or scarce. In addition, they could be replaced without significant cost, effort, or delay in the ability to continue producing outputs.
- IE82 Because none of the criteria in paragraph B12C is met, Purchaser concludes that the acquired set of activities and assets is not a business.

Scenario 3—Background

- IE83 Assume the same facts as in Scenario 2, except that the acquired set of activities and assets also includes the employees responsible for leasing, tenant management, and managing and supervising all operational processes.

Scenario 3—Application of requirements

- IE84 Purchaser elects not to apply the optional concentration test set out in paragraph B7B and therefore assesses whether the set meets the minimum requirements to be considered a business in accordance with paragraphs B8–B12D.
- IE85 The acquired set of activities and assets has outputs because it generates revenue through the in-place leases. Consequently, Purchaser applies the criteria in paragraph B12C.

- IE86 Purchaser concludes that the criterion in paragraph B12C(a) is met because the set includes an organised workforce with the necessary skills, knowledge or experience to perform processes (ie leasing, tenant management, and managing and supervising the operational processes) that are substantive because they are critical to the ability to continue producing outputs when applied to the acquired inputs (ie the land, buildings and in-place leases). Furthermore, Purchaser concludes that the criterion in paragraph B8 is met because those substantive processes and inputs together significantly contribute to the ability to create output. Consequently, Purchaser concludes that the acquired set of activities and assets is a business.

Example B—acquisition of a drug candidate

Scenario 1—Background

- IE87 An entity (Purchaser) purchases a legal entity that contains:
- (a) the rights to an in-process research and development project that is developing a compound to treat diabetes and is in its final testing phase (Project 1). Project 1 includes the historical know-how, formula protocols, designs and procedures expected to be needed to complete the final testing phase.
 - (b) a contract that provides outsourced clinical trials. The contract is priced at current market rates and a number of vendors in the marketplace could provide the same services. Therefore, the fair value associated with this contract is nil. Purchaser has no option to renew the contract.

No employees, other assets, other processes or other activities are transferred.

Scenario 1—Application of requirements

- IE88 Purchaser elects to apply the optional concentration test set out in paragraph B7B and concludes that:
- (a) Project 1 is a single identifiable asset because it would be recognised and measured as a single identifiable intangible asset in a business combination.
 - (b) because the acquired contract has a fair value of nil, substantially all of the fair value of the gross assets acquired is concentrated in Project 1.

- IE89 Consequently, Purchaser concludes that the acquired set of activities and assets is not a business.

Scenario 2—Background

- IE90 Assume the same facts as in Scenario 1 except that the acquired set of activities and assets also includes another in-process research and development project that is developing a compound to treat Alzheimer's disease and is in its final testing phase (Project 2). Project 2 includes the historical know-how, formula protocols, designs, and procedures expected to be needed to complete the final phase of testing. The fair value associated with Project 2 is similar to the fair value associated with Project 1. No employees, other assets, processes or other activities are transferred.

Scenario 2—Application of requirements

- IE91 Purchaser elects to apply the optional concentration test set out in paragraph B7B and concludes that:
- (a) Project 1 and Project 2 are identifiable intangible assets that would each be recognised and measured as a separate identifiable asset in a business combination.

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- (b) Project 1 and Project 2 are not similar identifiable assets because significantly different risks are associated with managing and creating outputs from each asset. Each project has significantly different risks associated with developing, completing and marketing the compound to customers. The compounds are intended to treat significantly different medical conditions, and each project has a significantly different potential customer base.
- (c) consequently, the fair value of the gross assets acquired is not substantially all concentrated in a single identifiable asset or group of similar identifiable assets. Therefore, Purchaser assesses whether the set meets the minimum requirements to be considered a business in accordance with paragraphs B8–B12D.

IE92 The acquired set of activities and assets does not have outputs because it has not started generating revenue. Thus, Purchaser applies the criteria in paragraph B12B. Purchaser concludes that those criteria are not met for the following reasons:

- (a) the set does not include an organised workforce; and
- (b) although the contract that provides outsourced clinical trials might give access to an organised workforce that has the necessary skills, knowledge or experience to perform processes needed to carry out the clinical trials, that organised workforce cannot develop or convert the inputs acquired by Purchaser into outputs. Successful clinical trials are a pre-condition for producing output, but carrying out those trials will not develop or convert the acquired inputs into outputs.

Consequently, Purchaser concludes that the acquired set of activities and assets is not a business.

Example C—acquisition of a biotech entity

Background

IE93 An entity (Purchaser) purchases a legal entity (Entity Biotech). Entity Biotech's operations include: research and development activities on several drug compounds that it is developing (in-process research and development projects); senior management and scientists who have the necessary skills, knowledge, or experience to perform research and development activities; and tangible assets (including a corporate headquarters, a research lab, and lab equipment). Entity Biotech does not yet have a marketable product and has not yet generated revenue. Each of the assets acquired has a similar fair value.

Application of requirements

IE94 It is evident that the fair value of the gross assets acquired is not substantially all concentrated in a single identifiable asset or group of similar identifiable assets. Thus, the optional concentration test set out in paragraph B7B would not be met. Consequently, Purchaser assesses whether the set meets the minimum requirements to be considered a business in accordance with paragraphs B8–B12D.

IE95 Purchaser first assesses whether it has acquired any processes. No process is documented. Nevertheless, the acquired organised workforce has proprietary knowledge of Biotech's ongoing projects and experience with them. Applying paragraph B7(b), Purchaser concludes that the intellectual capacity of the acquired organised workforce having the necessary skills and experience following rules and conventions provides the necessary processes that are capable of being applied to inputs to create outputs.

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- IE96 Purchaser next assesses whether the acquired processes are substantive. The set of activities and assets does not have outputs. Thus, Purchaser applies the criteria in paragraph B12B. Purchaser concludes that those criteria are met because:
- (a) the acquired processes are critical to the ability to develop or convert the acquired inputs into outputs; and
 - (b) the inputs acquired include both:
 - (i) an organised workforce that has the necessary skills, knowledge, or experience to perform the acquired processes; and
 - (ii) other inputs that the organised workforce could develop or convert into outputs. Those inputs include the in-process research and development projects.
- IE97 Finally, applying the criteria in paragraph B8, Purchaser concludes that the acquired substantive processes and the acquired inputs together significantly contribute to the ability to create output. Consequently, Purchaser concludes that the acquired set of activities and assets is a business.

Example D—acquisition of a television station

Background

- IE98 An entity (Purchaser) purchases broadcasting assets from another entity (Seller). The acquired set of activities and assets includes only the communications licence, the broadcasting equipment and an office building. Each of the assets acquired has a similar fair value. Purchaser does not purchase the processes needed to broadcast programmes and it does not acquire any employees, other assets, other processes or other activities. Before the acquisition date, Seller stopped broadcasting using the set of activities and assets acquired by Purchaser.

Application of requirements

- IE99 Purchaser elects to apply the optional concentration test set out in paragraph B7B and concludes that:
- (a) the broadcasting equipment and building are not a single identifiable asset because the equipment is not attached to the building and can be removed without significant cost or diminution in utility or fair value of either asset.
 - (b) the licence is an intangible asset, whereas the broadcasting equipment and building are tangible assets in different classes. Consequently, in accordance with paragraph B7B(f), the assets are not considered similar to each other.
 - (c) each of the single identifiable assets has similar fair value. Thus, the fair value of the gross assets acquired is not substantially all concentrated in a single identifiable asset or group of similar identifiable assets.

Consequently, Purchaser assesses whether the set of activities and assets meets the minimum requirements to be considered a business in accordance with paragraphs B8–B12D.

- IE100 The set of activities and assets does not have outputs, because Seller has stopped broadcasting. Thus, Purchaser applies the criteria in paragraph B12B. The set does not include an organised workforce, so it does not meet those criteria. Consequently, Purchaser concludes that the acquired set of activities and assets is not a business.

Example E—acquisition of a closed manufacturing facility

Background

IE101 An entity (Purchaser) purchases a closed manufacturing facility—the land and the building—as well as the related equipment. The fair value of the equipment and the fair value of the facility are similar. To comply with local laws, Purchaser must take over the employees who worked in the facility. No other assets, processes or other activities are transferred. The acquired set of activities and assets stopped producing outputs before the acquisition date.

Application of requirements

IE102 Purchaser elects to apply the optional concentration test set out in paragraph B7B and concludes that:

- (a) the equipment and the facility are not a single identifiable asset because the equipment could be removed from the facility without significant cost or diminution in utility or fair value of either the equipment or the facility—the equipment is not attached to the facility and can be used in many other types of manufacturing facilities.
- (b) the equipment and facility are not similar identifiable assets because they are in different classes of tangible assets.
- (c) the fair values of the equipment and the facility are similar. Therefore, the fair value of the gross assets acquired is not substantially all concentrated in a single identifiable asset or group of similar identifiable assets.

Consequently, Purchaser assesses whether the set of activities and assets meets the minimum requirements to be considered a business in accordance with paragraphs B8–B12D.

IE103 The acquired set of activities and assets does not have outputs at the acquisition date because it stopped producing outputs before then. Consequently, Purchaser applies the criteria in paragraph B12B. The set includes an organised workforce that has the necessary skills, knowledge or experience to use the equipment, but it does not include another acquired input (such as intellectual property or inventories) that the organised workforce could develop or convert into outputs. The facility and the equipment cannot be developed or converted into outputs. Consequently, Purchaser concludes that the acquired set of activities and assets is not a business.

Example F—licence of distribution rights

Background

IE104 An entity (Purchaser) purchases from another entity (Seller) the exclusive sublicense to distribute Product X in a specified jurisdiction. Seller has the licence to distribute Product X worldwide. As part of this transaction, Purchaser also purchases the existing customer contracts in the jurisdiction and takes over a supply contract to purchase Product X from the producer at market rates. None of the identifiable assets acquired has a fair value that constitutes substantially all of the fair value of the gross assets acquired. No employees, other assets, processes, distribution capabilities or other activities are transferred.

Application of requirements

IE105 Purchaser elects to apply the optional concentration test set out in paragraph B7B and concludes that:

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- (a) the identifiable assets that could be recognised in a business combination include the sublicense to distribute Product X, customer contracts and the supply contract;
- (b) the sublicense and customer contracts are in different classes of intangible assets, so they are not similar identifiable assets; and
- (c) consequently, the fair value of the gross assets acquired is not substantially all concentrated in a single identifiable asset or group of similar identifiable assets.

Consequently, Purchaser assesses whether the set of activities and assets meets the minimum requirements to be considered a business in accordance with paragraphs B8–B12D.

IE106 The set of activities and assets has outputs because at the acquisition date the licence was generating revenue from customers in the jurisdiction specified in the sublicense. Consequently, Purchaser applies the criteria in paragraph B12C. As explained in paragraph B12D(a), acquired contracts are an input and not a substantive process. Purchaser considers next whether the acquired supply contract provides access to an organised workforce that performs a substantive process. Because the supply contract is not providing a service that applies a process to another acquired input, Purchaser concludes that the substance of the supply contract is only that of buying Product X, without acquiring the organised workforce, processes and other inputs needed to produce Product X. Furthermore, the acquired sublicense is an input, not a process. Purchaser concludes that the set is not a business because it does not include an organised workforce and Purchaser has acquired no substantive process that could meet the criteria in paragraph B12C.

Example G—acquisition of brands

Background

IE107 Assume the same facts as in Example F, except that Purchaser purchases the worldwide rights to Product X, including all related intellectual property. The acquired set of activities and assets includes all customer contracts and customer relationships, finished goods inventories, marketing materials, customer incentive programmes, raw material supply contracts, specialised equipment specific to manufacturing Product X and documented manufacturing processes and protocols to produce Product X. No employees, other assets, other processes or other activities are transferred. None of the identifiable assets acquired has a fair value that constitutes substantially all of the fair value of the gross assets acquired.

Application of requirements

IE108 As noted in paragraphs IE105 and IE107, the fair value of the gross assets acquired is not substantially all concentrated in a single identifiable asset or group of similar identifiable assets. Thus, the optional concentration test set out in paragraph B7B would not be met. Consequently, Purchaser assesses whether the set of activities and assets meets the minimum requirements to be considered a business in accordance with paragraphs B8–B12D.

IE109 The set of activities and assets has outputs, so Purchaser applies the criteria in paragraph B12C. The set does not include an organised workforce and, therefore, does not meet the criterion in paragraph B12C(a). However, Purchaser concludes that the acquired manufacturing processes are substantive because, when applied to acquired inputs, such as the intellectual property, raw material supply contracts and specialised equipment, those processes significantly contribute to the ability to continue producing outputs and because they are unique to Product X. Consequently, the criterion in paragraph B12C(b) is met. Furthermore, Purchaser concludes that the criterion in paragraph B8 is met because those substantive processes and inputs together significantly contribute to the ability to create output. As a result, Purchaser concludes that the acquired set of activities and assets is a business.

Example H—acquisition of loan portfolio

Scenario 1—Background

IE110 An entity (Purchaser) purchases a loan portfolio from another entity (Seller). The portfolio consists of residential mortgage loans with terms, sizes and risk ratings that are not significantly different. No employees, other assets, processes or other activities are transferred.

Scenario 1—Application of requirements

IE111 Purchaser elects to apply the optional concentration test set out in paragraph B7B and concludes that:

- (a) the assets (residential mortgage loans) are similar in nature;
- (b) the risks associated with managing and creating outputs are not significantly different because the terms, sizes and risk ratings of the loans are not significantly different;
- (c) the acquired loans are similar assets; and
- (d) consequently, substantially all of the fair value of the gross assets acquired is concentrated in a group of similar identifiable assets.

Consequently, Purchaser concludes that the acquired set of activities and assets is not a business.

Scenario 2—Background

IE112 Assume the same facts as in Scenario 1 except that the portfolio of loans consists of commercial loans with terms, sizes and risk ratings that are significantly different. None of the acquired loans, and no group of loans with similar terms, sizes and risk ratings, has a fair value that constitutes substantially all of the fair value of the acquired portfolio. No employees, other assets, processes or other activities are transferred.

Scenario 2—Application of requirements

IE113 Purchaser elects to apply the optional concentration test set out in paragraph B7B and concludes that:

- (a) the assets (commercial loans) are similar in nature;
- (b) the risks associated with managing and creating outputs from the loans are significantly different because the terms, sizes and risk ratings of the loans are significantly different;
- (c) the acquired loans are not similar identifiable assets; and
- (d) consequently, the fair value of the gross assets acquired is not substantially all concentrated in a group of similar identifiable assets.

Consequently, Purchaser assesses whether the set meets the minimum requirements to be considered a business in accordance with paragraphs B8–B12D.

IE114 The portfolio of loans has outputs because it generates interest income. Consequently, Purchaser applies the criteria in paragraph B12C. Acquired contracts are not a substantive process, as explained in paragraph B12D(a). Moreover, the acquired set of activities and assets does not include an organised workforce and there are no acquired processes that

could meet the criteria in paragraph B12C(b). Consequently, Purchaser concludes that the acquired set of activities and assets is not a business.

Scenario 3—Background

- IE115 Assume the same facts as in Scenario 2 but Purchaser also takes over the employees of Seller (such as brokers, vendors, and risk managers) who managed the credit risk of the portfolio and the relationship with the borrowers. The consideration transferred to Seller is significantly higher than the fair value of the acquired portfolio of loans.

Scenario 3—Application of requirements

- IE116 As noted in paragraph IE113, the fair value of the gross assets acquired is not substantially all concentrated in a group of similar identifiable assets. Thus, the optional concentration test set out in paragraph B7B would not be met. Consequently, Purchaser assesses whether the set meets the minimum requirements to be considered a business in accordance with paragraphs B8–B12D.
- IE117 The portfolio of loans has outputs because it generates interest income. Consequently, Purchaser applies the criteria in paragraph B12C and concludes that the criterion in paragraph B12C(a) is met because the set includes an organised workforce with the necessary skills, knowledge or experience to perform processes (customer relationship management and credit risk management) critical to the ability to continue producing outputs. Furthermore, Purchaser concludes that the criterion in paragraph B8 is met because those substantive processes and the acquired inputs (the portfolio of loans) together significantly contribute to the ability to create output. Consequently, Purchaser concludes that the acquired set is a business.

Example I—determining the fair value of the gross assets acquired

Background

- IE118 An entity (Purchaser) holds a 20% interest in another entity (Entity A). At a subsequent date (the acquisition date), Purchaser acquires a further 50% interest in Entity A and obtains control of it. Entity A's assets and liabilities on the acquisition date are the following:
- (a) a building with a fair value of CU500;
 - (b) an identifiable intangible asset with a fair value of CU400;
 - (c) cash and cash equivalents with a fair value of CU100;
 - (d) financial liabilities with a fair value of CU700; and
 - (e) deferred tax liabilities of CU160 arising from temporary differences associated with the building and the intangible asset.
- IE119 Purchaser pays CU200 for the additional 50% interest in Entity A. Purchaser determines that at the acquisition date the fair value of Entity A is CU400, that the fair value of the non-controlling interest in Entity A is CU120 (30% x CU400) and that the fair value of the previously held interest is CU80 (20% x CU400).

Application of requirements

- IE120 To perform the optional concentration test set out in paragraph B7B, Purchaser needs to determine the fair value of the gross assets acquired. Applying paragraph B7B, Purchaser determines that the fair value of the gross assets acquired is CU1,000, calculated as follows:

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- (a) the fair value of the building (CU500); plus
 - (b) the fair value of the identifiable intangible asset (CU400); plus
 - (c) the excess (CU100) of:
 - (i) the sum (CU400) of the consideration transferred (CU200), plus the fair value of the non-controlling interest (CU120), plus the fair value of the previously held interest (CU80); over
 - (ii) the fair value of the net identifiable assets acquired (CU300 = CU500 + CU400 + CU100 – CU700).
- IE121 The excess referred to in paragraph IE120(c) is determined in a manner similar to the initial measurement of goodwill in accordance with paragraph 32 of SB-FRS 103. Including this amount in determining the fair value of the gross assets acquired means that the concentration test is based on an amount that is affected by the value of any substantive processes acquired.
- IE122 The fair value of gross assets acquired is determined after making the following exclusions specified in paragraph B7B(a) of SB-FRS 103 for items that are independent of whether any substantive process was acquired:
- (a) the fair value of the gross assets acquired does not include the fair value of the cash and cash equivalents acquired (CU100) and does not include deferred tax assets (nil in this example); and
 - (b) for the calculation specified in paragraph IE120(c)(ii), the deferred tax liability is not deducted in determining the fair value of the net assets acquired (CU300) and does not need to be determined. As a result, the excess (CU100) calculated by applying paragraph IE120(c) does not include goodwill resulting from the effects of deferred tax liabilities.
- IE123 The fair value of the gross assets acquired (CU1,000) may also be determined as follows:
- (a) the total (CU1,100) obtained by adding:
 - (i) the amount paid (CU200) (plus the fair value of the non-controlling interest (CU120) plus the fair value of the previously held interest (CU80)); to
 - (ii) the fair value of the liabilities assumed (other than deferred tax liabilities) (CU700); less
 - (b) the cash and cash equivalents acquired (CU100); less
 - (c) deferred tax assets acquired (nil in this example). In practice, it would be necessary to determine the amount of deferred tax assets to be excluded only if including the deferred tax assets could lead to the concentration test not being met.