Project	**Amendments to IFRS3 and IAS27**
Topic	**Acquisition-related costs in a business combination**

Proposed amendment

1. The IFRIC has received requests to clarify the treatment of acquisition-related costs that the acquirer incurred before the application of IFRS 3 (as issued in 2008) (IFRS 3R) that relate to a business combination that is accounted for according to the revised standard. Some constituents believe that IFRS 3R is not clear on whether those acquisition-related costs should be capitalised or expensed. Therefore, they ask the IFRIC to clarify the transition requirements.

Background

2. Acquisition-related costs are costs the acquirer incurs to effect a business combination. Those costs include for example advisory, legal, accounting, valuation and other professional or consulting fees.

3. IFRS 3.24 (as issued in 2004) required the acquirer to measure the cost of a business combination as the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the acquirer, in exchange for control of the acquiree plus any costs directly attributable to the business combination (acquisition-related costs). As a consequence, acquisition-related costs were generally capitalised as part of the measurement of goodwill or other assets acquired in the business combination.

4. IFRS 3R amends the treatment of acquisition-related costs. IFRS 3R.53 states that acquisition-related costs are expenses in the periods in which the costs are

incurred and the services are received, with one exception. The costs to issue debt or equity securities are recognised in accordance with IAS 32 and IAS 39.

5. IFRS 3R.64 states that the revised standard should be applied prospectively 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 July 2009. However, the revised standard does not contain transition requirements for acquisition-related costs. As a consequence, a question arises how acquisition-related costs that the acquirer incurred before the application of IFRS 3R that relate to a business combination that is accounted for according to the revised standard should be accounted for.

6. The following views have developed in practice:

View A: The acquisition-related costs should be expensed. Supporters of View A argue that IFRS 3R is applicable because the acquisition-related costs were incurred in respect to a business combination for which the acquisition date falls after the effective date of the revised standard.

View B1: The acquisition-related costs incurred in the reporting periods before adoption of the revised standard should be capitalised and those incurred after the revised standard is adopted should be expensed. Therefore, supporters of View B1 would first apply the requirements of IFRS 3 (as issued in 2004) and then upon adoption of IFRS 3R apply those requirements.

View B2: The acquisition-related costs incurred in the reporting periods before adoption of the revised standard should be capitalised. Upon adoption of the new standard, acquisition-related costs should be expensed retrospectively and comparative periods are restated. Supporters of View B2 argue that the adoption of IFRS 3R is a change in accounting principle and that therefore the requirements in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* should be applied.

View B3: The acquisition-related costs incurred in the reporting periods before adoption of the revised standard should be capitalised. However, upon adoption of IFRS 3R, the acquirer adjusts the opening balance of retained earnings without restatement of the comparative periods.

Staff Analysis

7. The staff considers that acquisition-related costs generally would not meet the definition of an asset on their own. Accordingly the question underlying Views A and B is whether the accounting for acquisition-related costs for a business combination is governed by (a) the standard that is effective when they are incurred, i.e. IFRS 3 (as issued in 2004), or (b) the standard that is used to account for the business combination, i.e. IFRS 3R.

8. In our view, an entity should account for acquisition-related costs in accordance with the standard that is used to account for the business combination because, even though the acquisition-related costs are not part of the exchange transaction, they are related to the business combination. Therefore, we believe that acquisition-related costs that the acquirer incurred before the adoption of IFRS 3R that relate to a business combination that is accounted for according to the revised standard, should be expensed, unless they are accounted for in accordance with IAS 32 and 39.

9. We believe that the requirement in IFRS 3.24 (as issued in 2004) to include acquisition-related costs in the measurement of the cost of a business combination applies only to business combinations that are accounted for in accordance with that standard and cannot be extended to other business combinations. The acquisition-related costs in question relate to business combinations that are not accounted for according to IFRS 3 (as issued in 2004). Therefore, we believe that the requirement in IFRS 3.24 (as issued in 2004) is not applicable.

Staff recommendation and question to the IFRIC

10. We believe that the treatment of acquisition-related costs that relate to a business combination that is accounted for in accordance with IFRS 3R that the acquirer incurred before adoption of the revised standard, can be determined with sufficient clarity from the withdrawal of IFRS 3 (as issued in 2004) and the explanations in IFRS 3R. Therefore, we recommend that the IFRIC does not add this issue to its agenda.

11. Proposed wording for the tentative agenda decision is set out in Appendix A.

Question to the IFRIC
Does the IFRIC agree with the staff recommendation not to add the issue to its agenda? If not, why? Does the IFRIC have any comments on the propsed wording of the tentative agenda decision?

[Appendix A has been omitted from this Observer note]