Project **Annual improvement — 2008 – 2010 Cycle**

Topic **IFRS 3 *business combinations* - Measurement of NCI – Illustrative examples**

Introduction

1. In January 2010 the IFRIC affirmed a proposed amendment to paragraph 19 of IFRS 3 (revised 2008) to clarify that the choice for measuring the non-controlling interest in the acquiree applies only to 'components of non-controlling interests that are present ownership instruments and entitle their holders to a proportionate share of the entity's net assets in the event of liquidation'. Other present ownership instruments that are classified as non-controlling interests should be measured 'at fair value, unless another measurement basis is required by IFRSs'[1].

2. The IFRIC also asked the staff to prepare examples that would illustrate the application of the requirement. In response to the IFRIC request, the staff has prepared some illustrative examples which are included in Appendix A of this paper.

[1] See *IFRIC Update* in January 2010: http://media.iasb.org/IFRICUpdateJan2010.html#5

Action to be taken by IFRIC members
Please, review the illustrative examples in Appendix A of this paper and let us know your comments.

Appendix A - Amendment to IFRS 3

Illustrative examples

A new heading is added after IE44 and paragraphs IE44A to IE44K are added:

Measurement of non-controlling interest

Illustrating the consequences of applying paragraph 19 of IFRS 3

IE44A The following examples illustrate the measurement of NCI at the acquisition date in a business combination.

Measurement of NCI including preference Shares

IE44B TC has issued 1,000 ordinary shares and 100 preference shares, which are classified as equity. The preference shares have a nominal value of CU1 each. The preference shares give their holders a right to a preferential dividend in priority to the payment of any dividend to the holders of ordinary shares. Upon liquidation of TC, the holders of the preference shares are entitled to receive out of the assets available for distribution the amount of CU1 per share in priority to the holders of ordinary shares. The holders of the preference shares do not have any further rights on liquidation.

IE44C AC acquires 800 ordinary shares of TC in exchange for CU1,200. The acquisition gives AC control of TC. The acquisition-date fair value of TC's identifiable net assets is CU1,400. The acquisition-date fair value of an ordinary share is CU1.5 and that of a preference share is CU1.2.

IE44D Paragraph 19 of IFRS 3 states that for each business combination, the acquirer shall measure at the acquisition date components of non-controlling interests in the acquiree that are present ownership interests and entitle their holders to a proportionate share of the entity's net assets in the event of liquidation at either fair value or the present ownership instruments' proportionate share in the acquiree's recognised amounts of the identifiable net assets. All other components of non-controlling interests shall be measured at their acquisition-date fair value, unless another measurement basis is required by IFRSs.

IE 44E AC can choose to measure the non-controlling interests that relate to TC's ordinary shares either at their fair value of CU300 (200 ordinary shares x CU1.5) or at their proportionate share in the acquiree's recognised amounts of the identifiable net assets of CU260 (200/1,000 ordinary shares x (CU1,400 - CU100).

IE44F The non-controlling interests that relate to TC's preference shares do not qualify for the measurement choice in paragraph 19 of IFRS 3 because they do not entitle their holders to a proportionate share of the entity's net assets in the event of liquidation. The acquirer must measure the preference shares at their acquisition-date fair value of CU120 (100 preference shares x CU1.2).

First variation

IE44G Suppose that upon liquidation of TC, the holders of the preference shares are entitled to receive a proportionate share of the assets available for distribution. The holders of the preference shares have equal right and ranking to the holders of ordinary shares in the event of liquidation. Assume that because of those rights the acquisition-date fair value of a preference share is now CU1.6 and the fair value of an ordinary share is CU1.4.

IE44H The preference shares qualify for the measurement choice in paragraph 19 of IFRS 3. AC can choose to measure the non-controlling interests either at their acquisition date fair value of CU440 (CU1.4 x 200 ordinary shares + CU1.6 x 100 preference shares) or at their proportionate share in the acquiree's recognised amounts of the identifiable net assets of CU382 (CU1,400 x (200 ordinary shares + 100 preference shares) / (1,000 ordinary shares + 100 preference shares)).

Second Variation

IE44I Suppose also that TC has issued share options as remuneration to its employees. The share options are classified as equity and unvested at the acquisition-date. The market-based measure of the share options in accordance with IFRS 2 *Share-based Payment* at the acquisition date is CU200. The share options do not expire on the acquisition-date and AC does not replace them.

IE44J The share options do not represent present ownership interest and do not entitle their holders to a proportionate share of TC's net assets in the event of liquidation. Therefore, paragraph 19 of IFRS 3 requires the share-based payment transaction to be measured at its acquisition-date fair value, unless another measurement basis is required by IFRSs. Paragraph 30 of IFRS 3 states that the acquirer must measure an equity instrument related to share-based payment transactions of the acquiree in accordance with the method in IFRS 2.

IE44K The acquirer measures the non-controlling interests that are related to the share options at their market-based measure of CU200.