

STAFF PAPER

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IASB Meeting

Project	Definition of a business		
Paper topic	Wording of the proposed amendments		
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Introduction

1. At their joint meeting in September 2015, the Board and the FASB discussed the FASB’s tentative decisions on how to clarify the definition of a business and related application guidance.
2. In October 2015, the Board discussed an analysis of the FASB’s proposals on how to improve the application of the definition of a business and decided to propose changes to IFRS 3 *Business Combinations* that are the same as the amendments proposed by FASB.
3. In November 2015, the FASB issued the Proposed Accounting Standards Update *Clarifying the Definition of a Business*.¹
4. In December 2015, the Board tentatively decided to:
 - (a) clarify, in the illustrative examples of the proposed amendments, that a building acquired and an in-place operating lease shall be considered a single asset for the evaluation of the ‘substantially all’ threshold;
 - (b) clarify, in the proposed amendments to the application guidance of IFRS 3, that an acquired outsourcing agreement may be considered to provide an organised workforce and that the acquirer should consider whether the

¹ The FASB Proposed Accounting Standards Update can be downloaded at this link http://www.fasb.org/jsp/FASB/Document_C/DocumentPage?cid=1176167640849&acceptedDisclaimer=true

organised workforce accessed through the acquired outsourcing agreements perform a substantive process;

- (c) explain, in the Basis for Conclusions of the proposed amendments, that when an entity acquires a supplier that then ceases generating revenues, because all output is consumed by the acquirer, the supplier would still be 'capable of' generating revenues, and so it might qualify as a business, if the other criteria are met; and
 - (d) add two illustrative examples on how to apply the proposed guidance in the financial sector and in the extractive industries sector.
5. In December 2015, the Board also instructed the staff to commence the balloting process for the Exposure Draft of the proposed amendments.

Objective

- 6. The objective of this paper is to ask Board members whether they agree with our proposal to expose amendments to the Application Guidance of IFRS 3 that are different from the wording exposed by FASB. For this reason, in the following paragraphs, we report our proposed wording changes.
- 7. We are sharing our proposed wording changes with FASB staff.
- 8. We think that our proposed amendments provide the same requirements as the FASB proposed amendments (except where there is already a difference between IFRS Standards and US GAAP).

Wording changes proposed by the staff

Rearrangement of the paragraphs

- 9. We have changed the order in which we have presented some of the paragraphs that are proposed to be added to the Application Guidance of IFRS 3, compared with the FASB ED. We have presented the paragraphs relating to the assessment of concentration of fair value before the proposed guidance on substantive processes. We are proposing this to reflect the order in which these paragraphs are to be applied

in practice (ie the proposed guidance on substantive processes should be considered only when the fair value of the assets acquired is not concentrated in a single asset or group of similar assets). The FASB ED, on the other hand, presents this guidance in the opposite order.

Explanation of gross assets acquired

10. The FASB ED includes the following paragraph (emphasis added):

*Notwithstanding the guidance in paragraphs 805-10-55-4 through 55-9, 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, the set is not considered a business.*

11. We propose to clarify in the proposed amendments to the application guidance of IFRS 3 that the ‘gross assets’ acquired comprise ‘identifiable and non-identifiable assets’. We propose this to explain that the fair value associated with any substantive processes acquired should be included in the fair value of the gross assets acquired, even though these substantive processes may not be recognised as identifiable assets. Similarly, the fair value of any assembled workforce acquired would also be included in the fair value of gross assets acquired..

Explanation about acquired contracts

12. The FASB ED includes the following paragraphs:

805-10-55-5C If a set has outputs, a continuation of revenues does not, on its own, indicate that both an input and a substantive process have been acquired. Accordingly, assumed contractual arrangements that provide for the continuation of revenues (for example, customer contracts, customer lists, and leases [when the set is the lessor]) should be excluded from the analysis in paragraph 805-10-55-5B of whether a process has been acquired.

805-10-55-5D For purposes of the analysis in paragraphs 805-10-55-5A through 55-5B, an organized workforce could consist of employees and/or certain contractual arrangements that take the place of

employees (for example, a property or asset management contract). An entity should consider whether the service provided through a contractual arrangement performs an acquired process (or group of processes) that is critical to the ability to create outputs when applied to another acquired input or inputs or if the contractual arrangement is an acquired input.

13. We propose to simplify the wording of these paragraphs to clarify that an acquired contract:

- (a) is not itself a substantive process;
- (b) may be an input; and
- (c) may give access to an organised workforce (eg through an outsourcing agreement). In this case, the acquirer should assess whether the outsourced workforce performs a substantive process and whether, as a result, the acquirer has acquired that substantive process.

14. We are proposing this, because we think that when the operation of a business has been outsourced and the acquirer takes over the outsourcing agreements, the acquirer should also assess whether it has acquired the substantive processes performed by the outsourced workforce, or whether the contract simply provides rights to receive services from the workforce that manages the business.

15. We think that this is relevant because in our (and FASB's) proposed amendments we are explaining that 'an organised workforce that has the necessary skills, knowledge or experience to perform an acquired process...' can represent a substantive process, as well as being an input. In other words, the intellectual capacity of an acquired organised workforce could be a substantive process; an example could be an organised group of research scientists.

Examples

16. We have included in our ED all of the examples included in the FASB ED; however, we have streamlined the wording of some illustrative examples, because, in our view, in some circumstances the FASB's examples are too detailed. We have not changed

the outcomes of the examples (except in respect of the example of a building acquired with an in-place lease, as decided by the Board in December 2015).

17. We also added an illustrative example on how to apply the proposed guidance in the financial sector. This was requested by the Board at the December 2015 Board meeting. The FASB ED does not include this example.

Staff recommendation

18. On the basis of the analysis above, we recommend that the Board should expose amendments to the Application Guidance of IFRS 3 that reflect these additional amendments, even though this will mean that the wording of our proposed amendment will be different from FASB’s proposed amendment.
19. We think that our proposed wording will provide the same requirements as the FASB ED (except where there is already a difference between IFRS and US GAAP) and could be clearer for our international stakeholders.

Questions for the Board members

Do Board Members have any questions about the additional wording changes we propose, and do you agree to expose amendments to the Application Guidance of IFRS 3 that are different from the wording exposed by FASB?