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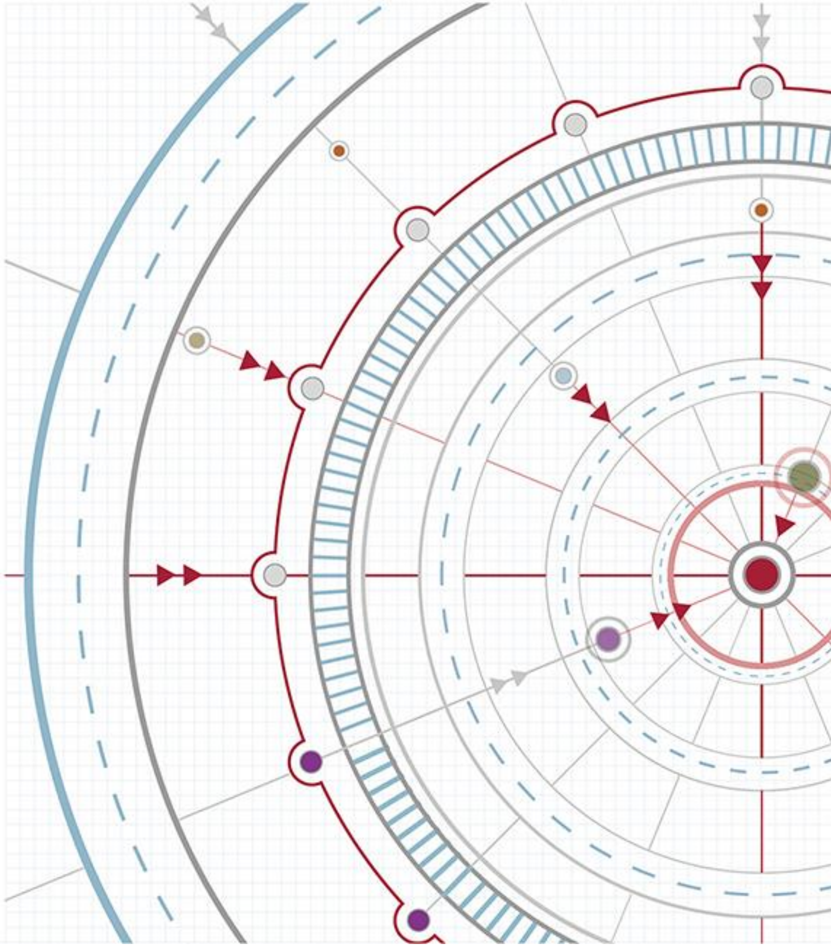

GPF meeting, 29 November 2016
Agenda Paper 4

# Definition of a Business

(Proposed amendments to IFRS 3 and IFRS 11)

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# Purpose of this session



- The exposure draft *Definition of a Business and Accounting for Previously Held Interests* (proposed amendments to IFRS 3 and IFRS 11) (the 'ED') was published in June 2016.
- Comment period ended 31 October 2016
- Purpose is to understand and discuss GPF members views on the proposed amendments

# Background



- The challenge of applying the definition of a business is a primary concern with IFRS 3 raised in the post-implementation review (PIR):
  - the definition of a business is broad;
  - preparers have difficulty assessing the relevance of processes acquired;
  - applying the definition of a business is especially challenging when the entity acquired generates no revenue;
  - the Standard provides little or no guidance on when a set of assets does not constitute a business; and
  - the Standard does not define the term ‘market participant’.

# Our proposed solutions – amendments to key concepts



- An acquisition must include:
  - an input and a substantive process that together contribute to the entity's ability to create outputs.
    - 'contribute' means that to be defined as a business, the set of assets acquired need not include all inputs and processes necessary for creating outputs.
    - A market participant's ability to integrate the acquired set of assets is no longer a consideration.
- The new definition of outputs:
  - focuses on goods and services provided to customers (like IFRS 15 *Revenue from Contracts with Customers*);
  - includes investment income and other revenue;
  - excludes other economic benefits provided to investors, other owners, members or participants;
  - excludes returns in the form of lower costs.

# Our proposed solutions – Two-stage assessment



## New assessments to simplify applying IFRS 3

**Assessment 1:**
**Evaluate concentration of fair value**

Is substantially all of the fair value of the gross assets acquired concentrated in a single asset or group of similar assets?

**Yes** → **Not a business**

**No** ↓

**Assessment 2:**
**Evaluate whether an acquired process is substantive**

Does the set of assets include an input and a substantive process that contribute to the ability to create outputs?

**No** → **Not a business**

**Yes** ↓

**Business**

# Our proposed solutions – Screening test



## Assessment 1—evaluate the concentration of fair value

- Is substantially all of the fair value of the gross assets acquired concentrated in a single asset or group of similar assets?
  - substantive process likely to have more than an insignificant fair value.
  - if substantially all of the fair value of the gross assets acquired is concentrated in a single asset, or group of similar assets, it is unlikely that a substantive process has been acquired.
- Gross assets acquired include any acquired input, contract, process, workforce and any other intangible asset that is not identifiable.
- The fair value of the gross assets acquired may be determined by adding the fair value of the liabilities assumed to the fair value of the consideration paid.

# Our proposed solutions – Screening test



**Assessment 1—evaluate the concentration of fair value**

Single asset:

- any items that would be recognised as a single asset in a business combination; and
- a tangible asset that cannot be physically removed and used separately from other tangible assets.

The following are not groups of similar assets:

- tangible and intangible assets;
- different classes of tangible assets;
- different classes of intangible assets;
- financial assets and non-financial assets; and
- different classes of financial assets.

# Questions for GPF members – Screening test



- Do you think the screening test is practical and helpful? Why or why not?
- Do you have any concerns about the operationality of the screening test?

# Our proposed solutions – Assessing substantive processes

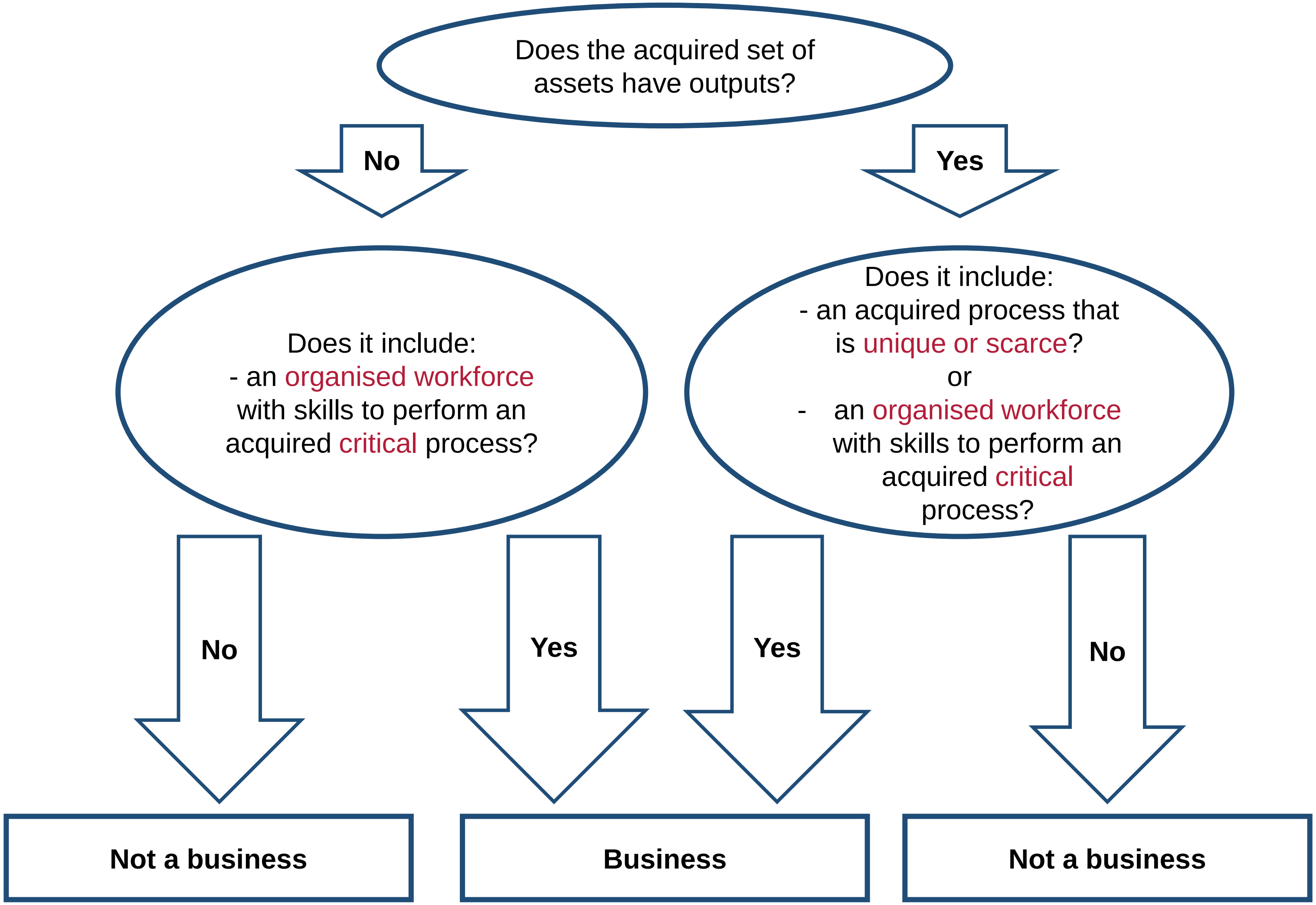


- Does the set of assets include an input and a substantive process that contributes to the ability to create outputs?

- Why provide guidance on evaluating whether an acquired process is substantive?
  - acquiring a substantive process that contributes to the ability to create outputs is necessary for a transaction to be a business combination.
  - assessing whether such a process has been acquired is one of the main challenges in applying the definition of a business.

# Our proposed solutions – Assessing substantive processes





# Our proposed solutions – Assessing substantive processes



## Assessment 2—evaluate whether an acquired process is substantive

- If the set does not have outputs, the set is a business only if it includes:
  - an organised workforce with the necessary skills to perform an acquired substantive process; **and**
  - the acquired substantive process that is critical to converting another acquired input into outputs.
- A process is not critical if it is ancillary or minor within the context of all the processes required to create outputs.
- Inputs that the workforce can convert into outputs include:
  - intellectual property;
  - other economic resources that can be developed to create outputs;
  - rights to access materials that allow the creation of outputs.

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# Our proposed solutions – Assessing substantive processes



## Assessment 2—evaluate whether an acquired process is substantive

- If the set has outputs, the set is a business if it includes:
  - – an organised workforce with the necessary skills to perform an acquired process that is critical to continue producing outputs; **or**
  - – a process:
    - – that contributes to the ability to continue producing outputs; and
    - – is unique or scarce, or cannot be replaced without significant cost, effort, or delay in the ability to continue producing outputs (ie a workforce is not required)

# Questions for GPF members – Assessing substantive processes



- Do you think having different criteria depending on whether the acquired set has outputs is helpful? Why or why not?
- Do you have any concerns about the operationality of this assessment?

# Our proposed solutions – Illustrative examples



## Add examples

- The ED includes 11 examples to illustrate the proposed guidance.
- The examples cover different industries, including:
  - real estate
  - pharmaceutical
  - broadcasting
  - manufacturing
  - technology
  - oil & gas
  - banking

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