IFRS EDUCATION SERIES

Business Combinations

IFRS 3

Including the Latest Amendments and IASB Developments

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ROADMAP

Contents

A structured walk-through of the acquisition method, special situations, and the latest amendments and proposals under IFRS 3

PART I

Foundations

Objective, scope, and the definition of a business under IFRS 3

OBJECTIVE

What IFRS 3 Requires

IFRS 3 establishes principles and requirements for how an acquirer:

1. **Recognises and measures** the identifiable assets acquired, liabilities assumed, and any non-controlling interest in the acquiree
2. **Recognises and measures** the goodwill acquired in the business combination, or a gain from a bargain purchase
3. **Determines what to disclose** to enable users of the financial statements to evaluate the nature and financial effects of the business combination

SCOPE

What IFRS 3 Does Not Cover

IFRS 3 applies to transactions meeting the definition of a business combination, but excludes:

Joint Arrangement Formation

The accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself

Common Control Combinations

Combinations of entities or businesses under common control, where all parties are ultimately controlled by the same party before and after

Asset Acquisitions

Acquisition of an asset or a group of assets that does not constitute a business, accounted for under the relevant asset-specific standards

KEY DEFINITION – 2018 AMENDMENT

What Is a Business?

A business is an integrated set of activities and assets capable of being conducted and managed to provide goods or services to customers, generate investment income, or generate other income from ordinary activities.

Inputs

Economic resources that create outputs when one or more processes are applied – e.g. non-current assets, intellectual property, employees

Process

A system, standard, protocol, convention or rule that, when applied to inputs, creates outputs – typically an organised workforce

Outputs

The result of inputs and processes applied to those inputs – goods or services to customers, investment income, or other income

KEY DEFINITION – 2018 AMENDMENT

The Optional Concentration Test

WHAT THE TEST DOES

An entity may elect to apply a simplified screening test: if substantially all of the fair value of the gross assets acquired is concentrated in a single identifiable asset (or group of similar assets), the acquired set is not a business – no further assessment is required.

WHY IT MATTERS

The test was introduced because entities were finding it costly and complex to assess whether a set of activities and assets met the definition of a business. Passing the test allows an entity to conclude directly, without evaluating inputs, processes and outputs in detail.

PART II

The Acquisition Method

The four steps every business combination is accounted for under IFRS 3

OVERVIEW

Four Steps of the Acquisition Method

Every business combination within the scope of IFRS 3 is accounted for by applying the acquisition method:

1. **Identify the acquirer** the entity that obtains control of the acquiree
2. **Determine the acquisition date** the date on which the acquirer obtains control of the acquiree
3. **Recognise and measure** the identifiable assets acquired, liabilities assumed, and any non-controlling interest
4. **Recognise and measure** goodwill or a gain from a bargain purchase

STEP 1

Identifying the Acquirer

For each business combination, one of the combining entities is identified as the acquirer – the entity that obtains control, applying the control guidance in IFRS 10.

Control-Based Test

The acquirer is identified by reference to IFRS 10's definition and guidance on control, not merely legal form

Reverse Acquisitions

Sometimes the legal acquirer is the accounting acquiree – for example, when a smaller entity arranges to be legally acquired by a larger one to obtain a stock exchange listing

STEP 2

Determining the Acquisition Date

DEFINITION

The acquisition date is the date on which the acquirer obtains control of the acquiree – generally the closing date, on which the acquirer legally transfers consideration, acquires the assets, and assumes the liabilities of the acquiree.

WHEN IT CAN DIFFER

Control may pass before or after the closing date – for example, under a written agreement that gives the acquirer control before closing. All facts and circumstances are considered in identifying the acquisition date.

STEP 3

The Recognition Principle

As of the acquisition date, the acquirer recognises, separately from goodwill, the identifiable assets acquired, liabilities assumed, and any non-controlling interest.

A **Meets the definitions** the assets and liabilities must meet the Conceptual Framework's definitions of assets and liabilities at the acquisition date

B **Part of the exchange** the assets and liabilities must be part of what the acquirer and acquiree exchanged in the business combination, rather than the result of a separate transaction

CLASSIFICATION

The acquirer classifies and designates identifiable assets acquired and liabilities assumed on the basis of the contractual terms, economic conditions, and other pertinent conditions as they exist at the acquisition date.

STEP 3

The Measurement Principle

Identifiable assets acquired and liabilities assumed are measured at their acquisition-date fair values, subject to limited exceptions:

Income Taxes

Deferred tax assets and liabilities are recognised and measured under IAS 12, not at fair value

Employee Benefits

Liabilities and assets for employee benefit arrangements are measured under IAS 19

Indemnification Assets

Measured on the same basis as the indemnified item, subject to a valuation allowance for collectability

Share-Based Payment

Replacement awards are measured in accordance with IFRS 2, not at fair value under IFRS 13

Assets Held for Sale

Non-current assets classified as held for sale are measured at fair value less costs to sell under IFRS 5

Reacquired Rights

Measured on the basis of the remaining contractual term, regardless of potential renewal

STEP 4

Recognising Goodwill or a Bargain Purchase

GOODWILL – THE FORMULA

Goodwill = (Consideration transferred + Amount of any non-controlling interest + Fair value of any previously held equity interest) – Net identifiable assets acquired (at fair value)

BARGAIN PURCHASE

If the result is negative, the acquirer first reassesses whether it has correctly identified all assets and liabilities, then recognises the resulting gain immediately in profit or loss.

STEP 4 – IN DETAIL

Goodwill Calculation Format

The build-up below is the standard working format used to compute goodwill on acquisition, illustrated with representative figures.

Component	Illustration ($)
Consideration transferred by the acquirer	50,000,000
(+) Non-controlling interest (at fair value or proportionate share)	12,000,000
(+) Fair value of any previously held equity interest (step acquisitions only)	–
= Total	62,000,000
(–) Fair value of identifiable net assets acquired	(55,000,000)
= Goodwill recognised	7,000,000

READING THE RESULT

Because the total of consideration and NCI ($62m) exceeds the fair value of identifiable net assets ($55m), the entity recognises the $7m difference as goodwill – an asset representing future economic benefits not individually identified and separately recognised.

STEP 4 – IN DETAIL

Bargain Purchase Calculation Format

The same build-up is used to test for a bargain purchase – the outcome differs only in which direction the balance falls.

Component	Illustration ($)
Consideration transferred by the acquirer	40,000,000
(+) Non-controlling interest (at fair value or proportionate share)	10,000,000
(+) Fair value of any previously held equity interest (step acquisitions only)	–
= Total	50,000,000
(–) Fair value of identifiable net assets acquired	(58,000,000)
= Bargain purchase gain	8,000,000

READING THE RESULT

Here the fair value of identifiable net assets ($58m) exceeds the total of consideration and NCI ($50m). After reassessing that all assets and liabilities have been correctly identified and measured, the entity recognises the $8m difference as a gain in profit or loss on the acquisition date.

PART III

Special Situations

Non-controlling interests, step acquisitions, contingent consideration, acquisition costs, and the measurement period

NCI

Measuring Non-Controlling Interests

For each business combination, the acquirer elects – on an acquisition-by-acquisition basis – to measure any non-controlling interest at:

Fair Value

The full goodwill method – NCI is measured at its acquisition-date fair value, which typically includes NCI's share of goodwill

Proportionate Share

The partial goodwill method – NCI is measured at its proportionate share of the acquiree's identifiable net assets, excluding any goodwill

BUSINESS COMBINATIONS ACHIEVED IN STAGES

Step Acquisitions

- Where the acquirer held an equity interest in the acquiree immediately before obtaining control (for example, an associate or a joint venture), the business combination is achieved in stages
- The acquirer remeasures its previously held equity interest to its acquisition-date fair value, and recognises the resulting gain or loss in profit or loss
- The remeasured fair value of the previously held interest is included as part of the consideration for the business combination when computing goodwill
- Any amounts previously recognised in other comprehensive income relating to the previously held interest are reclassified as if the acquirer had disposed of it directly

CONSIDERATION TRANSFERRED

Contingent Consideration

Consideration transferred includes the acquisition-date fair value of any contingent consideration – an obligation to transfer additional assets or equity interests if specified future events occur.

Classified as a Liability

Subsequently remeasured at fair value each period, with the change recognised in profit or loss

Classified as Equity

Not remeasured – subsequent settlement is accounted for within equity

COSTS

Acquisition-Related Costs

GENERAL RULE

Costs the acquirer incurs in connection with a business combination – finder's fees, advisory, legal, accounting, valuation and other professional or consulting fees, and general administrative costs – are expensed as incurred, in the periods in which the costs are incurred and the services received.

ONE EXCEPTION

Costs to issue debt or equity securities are recognised in accordance with IFRS 9 and IAS 32 respectively – not expensed, and not included in the cost of the business combination.

The Measurement Period

1. **Provisional amounts are permitted** if initial accounting for a business combination is incomplete by the end of the reporting period in which it occurs

2. **Retrospective adjustment** provisional amounts are adjusted retrospectively to reflect new information about facts and circumstances that existed at the acquisition date

3. **One-year limit** the measurement period ends as soon as the acquirer receives the information it was seeking, or learns that no more is obtainable – but cannot exceed one year from the acquisition date

PART IV

Latest Amendments & Developments

Reference to the Conceptual Framework, the pending disclosures project, and the impact of IFRS 18

FINALISED AMENDMENT

Reference to the Conceptual Framework (May 2020)

Effective for business combinations with an acquisition date on or after 1 January 2022, with early application permitted.

Updated Reference

IFRS 3 now refers to the Conceptual Framework issued in March 2018, replacing the reference to the 1989 Framework, without significantly changing the accounting requirements

IAS 37 / IFRIC 21 Exception Added

For liabilities and contingent liabilities within the scope of IAS 37 or IFRIC 21, the acquirer applies those standards – not the Conceptual Framework – to identify what has been assumed, avoiding potential 'day 2' gains or losses

Contingent Assets Clarified

The amendment explicitly states that an acquirer does not recognise contingent assets acquired in a business combination

UNDER REDELIBERATION – NOT YET FINALISED

Business Combinations – Disclosures, Goodwill and Impairment

The IASB published an Exposure Draft in March 2024 proposing amendments to IFRS 3 and IAS 36, following its post-implementation review of IFRS 3. As of mid-2026 the IASB is still redeliberating feedback, with a decision on project direction expected in Q4 2026 — nothing has yet been finalised.

Performance & Synergy Disclosures

The core proposal: disclosing post-acquisition performance information and expected synergies for a defined subset of business combinations, to address concerns that impairment arrives 'too little, too late'

Strategic Rationale Disclosure

Proposed to replace the current requirement to disclose the primary reasons for a combination with a broader strategic rationale disclosure

Contribution of the Acquired Business

Proposed to clarify that the profit or loss disclosed is operating profit or loss as defined in IFRS 18, and that the basis for combined entity information is an accounting policy

Impact of IFRS 18 on Presentation

IFRS 18 Presentation and Disclosure in Financial Statements replaces IAS 1 and is effective for annual periods beginning on or after 1 January 2027, with early application permitted.

- IFRS 18 introduces defined categories – operating, investing, financing – and required subtotals within the statement of profit or loss
- Acquisition-related costs expensed under IFRS 3, and gains or losses on remeasuring a previously held equity interest, are generally classified within the OPERATING category by default, unless they relate to an investing or financing activity
- Where an entity discloses a management-defined performance measure that excludes or adjusts for acquisition-related items, IFRS 18 requires a reconciliation to the most directly comparable IFRS-defined subtotal, together with an explanation of why the adjusted measure is useful
- IFRS 18 does NOT change the recognition or measurement requirements of IFRS 3 – its impact is confined to where acquisition-related line items are presented, and how non-GAAP adjusted measures must be reconciled

PART V

Worked Illustration

Computing goodwill in a straightforward business combination

ILLUSTRATION

Computing Goodwill on Acquisition

FACT PATTERN

Parent Co acquires 80% of the voting shares of Sub Co on 1 January 2026, obtaining control on that date.

Parent Co transfers cash consideration of $9,000,000 and issues shares with an acquisition-date fair value of $1,500,000 to the former shareholders of Sub Co.

At the acquisition date, the fair value of Sub Co's identifiable net assets is $8,000,000. Parent Co elects to measure the non-controlling interest (the remaining 20%) at its acquisition-date fair value of $1,900,000.

Required: Compute the goodwill arising on this business combination.

ILLUSTRATION

Solution

Component	Amount
Cash consideration transferred	$9,000,000
Fair value of shares issued	$1,500,000
Fair value of non-controlling interest (20%)	$1,900,000
Total	$12,400,000
Less: Fair value of identifiable net assets acquired	($8,000,000)
Goodwill	$4,400,000

SUMMARY

Key Takeaways

Acquisition Method, Always

Every in-scope business combination is accounted for using the same four-step method

Business vs. Asset Group

The 2018 definition and optional concentration test determine whether IFRS 3 applies at all

Goodwill Is a Residual

Consideration plus NCI plus any previously held interest, less identifiable net assets at fair value

NCI Has Two Measurement Bases

Fair value (full goodwill) or proportionate share (partial goodwill), elected per acquisition

2020 Amendment Is Narrow-Scope

Updates the Conceptual Framework reference, but IAS 37/IFRIC 21 govern liabilities and contingent liabilities

Bigger Changes Are Still Pending

The disclosures, goodwill and impairment project remains under IASB redeliberation

ABOUT THE AUTHOR

A Career Built on Making IFRS Understandable

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B D Chatterjee is a Chartered Accountant and financial thought leader with over 35 years of global experience spanning corporate finance, accounting standards, financial reporting, business valuation and financial due diligence. As a seasoned CFO, he has led finance functions across major corporations and now heads Digital CFO Solutions, a platform delivering institutional-grade IFRS, US GAAP and valuation workbooks alongside fractional CFO services.

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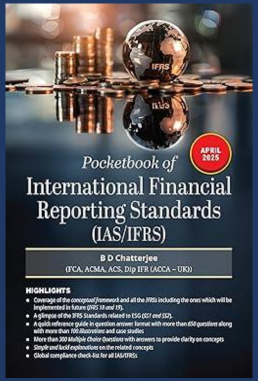
Books by B D Chatterjee — IFRS Library



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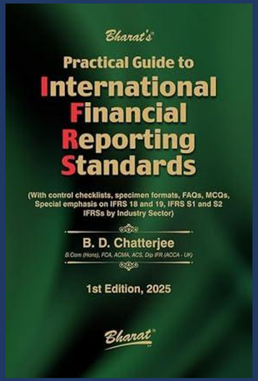

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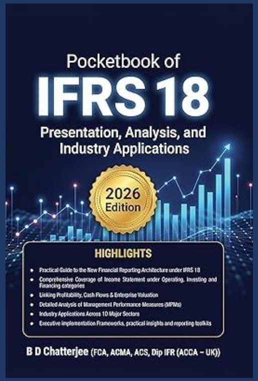
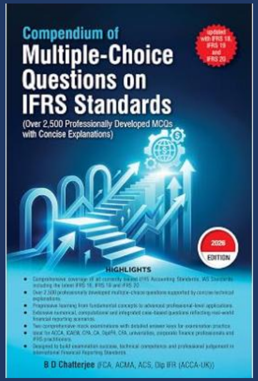
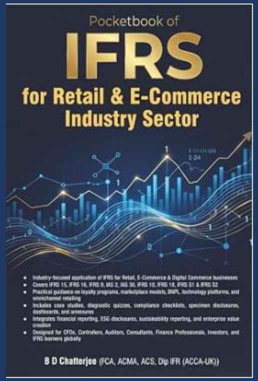


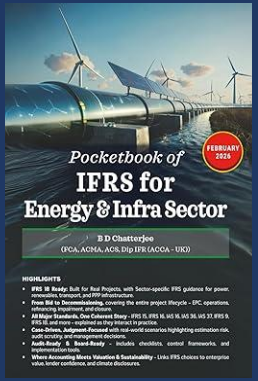
Pocketbook of IFRS 18 — Presentation, Analysis & Industry Applications



Compendium of Multiple-Choice Questions on IFRS Standards



Pocketbook of IFRS for Retail & E-Commerce Industry Sector



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