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Business Combinations and Consolidation

Second Edition

Tan Liong Tong

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Dedication to My

Wife	:	*Lee Guat Keow*
Sons	:	*Tan Hanxuan and Tan Hanyi*
Daughters	:	*Tan Xiaowen and Tan Xiaoqi*

ABOUT THE AUTHOR

Mr. Tan Liong Tong currently serves as a Technical Consultant to Mazars Malaysia. He is also the current project manager of the MASB Working Group on Consolidation. He is member of the Malaysian Institute of Certified Public Accountants (MICPA), the Malaysian Institute of Accountants (MIA) and an Associate Fellow of the Institute of Bankers Malaysia (IBBM). He was previously an Associate Professor at the Graduate School of Management, Universiti Putra Malaysia.

Mr. Tan has served in various working committees of the Malaysian professional accountancy bodies, including being a Council member of the MICPA, a member of its Accounting and Auditing Technical Committee, and a member of the Accounting & Auditing Standards Committees of the MIA. He was previously engaged as a Technical Consultant to the Malaysian Accounting Standards Board (MASB) and the Securities Commission (SC), and as a Technical Advisor to the Financial Reporting Standards Implementation Committee (FRSIC) of the MIA. He was a member of the Editorial Panel of the Institute of Bankers' Journal. He had also served as an external or chief examiner, an academic advisor, a consultant to various institutions and organisations, and as a project manager for various working groups of the MASB that developed MASB Standards.

Mr. Tan holds a Diploma in Agriculture and a Bachelor of Science in Agribusiness, both from Universiti Putra Malaysia. He also holds a Master in Business Administration from the University of Philippines, Diliman campus. He qualified as a CPA under articleship with an international accounting firm in Kuala Lumpur. His distinguished academic achievements include winning the Chancellor's Gold Medal for being the best overall student in Universiti Putra Malaysia and the Best Overall Performance awards in the MICPA's Foundation and Professional II examinations.

Mr. Tan's research interest lies in the area of financial accounting and reporting practices. He has published numerous research articles, books and monographs in this area of accounting. Apart from this Book, he has also authored and co-authored various books and manuals, including the popular titles of:

(1) *Consolidated Financial Statements, 6th edition*,

(2) *Financial Accounting & Reporting in Malaysia, Volumes I & II, 4th edition*,

(3) *Financial Instruments: Recognition, Measurement, Presentation & Disclosures, 2nd edition*,
(4) *A Practical Guide to Deferred Taxation*,
(5) *Share Buybacks and Financial Assistance*,
(6) *Financial Management*,
(7) *Deferred Taxation*,
(8) *An Application Handbook on MASB 25, Income Taxes*,
(9) *An Application Handbook on FRS 136, Impairment of Assets*,
(10) *An Application Handbook on FRS 111, Construction Contracts & FRS 201, Property Development Activities*, and
(11) *AccMan Malaysia – The Accountant's Manual.*

PREFACE

In May 2011, the International Accounting Standards Board (IASB) simultaneously issued six IFRSs, of which five relate to the subject of consolidation and one on fair value measurement. The five IFRSs related to consolidation are:

(i) IFRS 10, Consolidated Financial Statements;
(ii) IFRS 11, Joint Arrangements;
(iii) IFRS 12, Disclosures of Interests in Other Entities;
(iv) IAS 27(revised), Separate Financial Statements; and
(v) IAS 28(revised), Investments in Associates and Joint Ventures.

IFRS 10 replaces the consolidation part of the former IAS 27. IAS 27(revised) deals only with accounting for investments in subsidiaries, joint ventures and associates in the separate financial statements of an investor (retains the part on separate financial statements in the former IAS 27). IFRS 11 supersedes the former IAS 31 on accounting for joint arrangements. Disclosure requirements on subsidiaries, joint arrangements, associates and involvement in unconsolidated structured entities are dealt with in IFRS 12.

The revised IFRS $3_{(2008)}$ permits non-controlling interests to be measured at fair value at the acquisition date. Consequently, an acquirer shall measure the acquiree as a whole and goodwill attributable to non-controlling interests shall be recognised. Furthermore, the new IFRS make greater use of fair value by requiring that any previously held interest in an investee shall be measured at fair value at the acquisition date, and the change in fair value, including gains or losses previously recognised in other comprehensive income and deferred in equity, shall be recognised in profit or loss on remeasurement when the increase in stake occurs. Any further increase in stake after the acquisition date shall be treated as an equity transaction.

IFRS 10 introduces a new single control model to identify a parent-subsidiary relationship. In this new control model, an investor controls an investee if and only if the investor has the three elements of (i) power, (ii) returns, and (ii) the link between power and returns. The implication on practice is that an investor may control another entity regardless of the extent of its ownership in the other entity (for example, control may be obtained by having sufficient voting rights or by contractual arrangements). For a decrease in stake that does not result in loss of control, IFRS 10 requires that it shall be treated as an equity transaction between the parent (controlling) interest and the non-controlling interests. Consequently, no gain or loss shall be recognised in profit or loss. When a loss of control occurs, a parent recognises the gain or loss in profit or loss, and this includes remeasurement to fair value, any stake retained in a former subsidiary and reclassification adjustments of previously recognised gains and losses in other comprehensive income (i.e. the recycling of reserves to profit or loss). Also, the IFRS requires that losses shall be allocated in full to non-controlling interest even of it results in a deficit to the non-controlling interest in the statement of financial position.

IFRS 11 requires that the accounting for joint arrangements shall focus on the economic substance of an arrangement. It uses a rights and obligation approach in which parties to an arrangement recognise their respective rights and obligations arising from the arrangement. It removes the proportionate consolidation method in the former IAS 31 and requires the use of the equity method if the arrangement is a joint venture. For a joint operation, the IFRS requires a joint operator to account for the assets, liabilities, revenue and expenses directly based on its rights and obligations.

There are no significant changes to the accounting in the separate financial statements of a parent or an investor in the revised IAS 27. Investments in subsidiaries, joint ventures and associates are either accounted for at cost or a fair value through profit or loss. IAS 28 (revised) now includes equity accounting requirements for joint ventures. It also provides guidance on changes in stakes that result from discontinuation of the equity method.

These new and revised IFRSs bring about significant changes to some current practice. The consolidation techniques used currently will need to be modified to suit these changes. Thus, it is essential that readers are aware of the principles that have been prescribed in these new and revised IFRSs.

The purpose of this book is to help accounting practitioners and students keep up to date with the subjects of accounting for business combinations and consolidation. The second edition of the book has incorporated the requirements of the new IFRSs. It is an issue-based book that focuses on the application aspects of the requirements of the IFRSs.

There are four chapters in this book and each chapter begins with some learning objective. The first chapter is on business combinations and it focuses on the application aspects of the standards prescribed in IFRS 3. The second chapter is devoted entirely to the application of reverse acquisition accounting, a relatively new method of accounting for business combinations in many countries. Chapter 3 is on consolidation and it discusses the standards prescribed in IFRS 10 and the revised IAS 27. Chapter 4 focuses on accounting for joint arrangements, associates and disclosures of interests on other entities, including disclosure of involvement in unconsolidated structured entities. Each chapter provides explanations, illustrations, worked examples and cases on the application aspects of the standards prescribed. Some practice cases are also provided at the end of each chapter

I am particularly grateful to my wife and children, for without their moral support and patience, the drafting of this book would not have been possible.

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