14 BUSINESS ACCOUNTING STANDARD “BUSINESS COMBINATIONS”


I. GENERAL PROVISIONS

1. The objective of this Standard is to set out how business combinations shall be recorded in accounting and presented in financial statements.

2. This Standard shall be applied in accounting for business combinations when:
   2.1. one entity obtains control over another entity;
   2.2. one entity, that intends to continue the operations of another entity, obtains control over all or part of assets of that other entity and assumes all or part of its liabilities (hereinafter, acquisition of a business);
   2.3. two or more entities are reorganised to combine them into one entity.

3. Except for provisions on measuring and accounting for goodwill, this Standard is not applicable for accounting for investments into associates and jointly controlled entities because under this Standard such acquisitions are not recognised as business combinations.

II. KEY DEFINITIONS

Replacement cost – the amount payable for the creation, manufacturing or construction (installation) or acquisition of an object of the same physical and operational qualities.

Settlement day – the day of full or partial payment for acquired net assets or equity instruments of an entity.

Carrying amount – the amount at which an asset, equity and liability is presented in the balance sheet.

Entity under common control – an entity controlled (managed) by the same legal or natural persons (their groups) and that control is not transitory.

Subsidiary – an entity that is controlled by another entity.

Net assets – the difference in the fair values of total assets and total liabilities.

Acquisition of an entity – a business combination in which one of the entities, the acquirer, obtains control over the net assets and operations of another entity, the acquiree, in exchange for the transfer of assets, assumption of liabilities, or emission of equity instruments.

Entity acquisition date – the date on which the acquirer obtains control over another entity.

Reorganisation of entities by way of merger – the bringing together of one or more entities into one entity.

Acquirer – an entity which merges with another entity (the acquiree) or obtains control over the net assets and operations thereof.

Acquiree – an entity which is merged with another entity (the acquirer) and ceases operating as a legal person or its operations fall under control of another entity.

Control – an entity’s power to govern another entity so as to obtain benefits from its activities. The control may be either direct or indirect.
Minority interest – the portion of net assets presented in the balance sheet or profit or loss presented in the income statement of the reporting period attributable to equity interests that are not owned, directly or indirectly through subsidiaries, by the parent.

Negative goodwill – the amount by which the price paid by the acquirer is lower than the value of the acquired interest in net assets of the acquired entity or the value of net assets of the acquired business.

Equity instruments – shares, member shares, depository warrants and other equity securities that give the acquirer the following rights:
- to participate in the management of the entity;
- to receive a share of profit of the entity;
- to receive a share of assets of the entity upon its liquidation;
- to transfer the equity securities owned.

Investment units of a collective investment fund are also attributed to equity instruments.

Parent – an entity that has one or more subsidiaries.

Goodwill – the amount by which the price paid by the acquirer exceeds the value of the acquired interest in net assets of the acquired entity or the value of net assets of the acquired business, and from which the acquirer expects to obtain future economic benefits.

Fair value – the amount for which an asset or service could be exchanged, or a liability settled between knowledgeable, willing parties in an arm’s length transaction.

Acquisition of a business – a business combination in which one entity, that intends to continue the operations of another entity, obtains control over all or part of assets of that other entity and assumes all or part of its liabilities in exchange for the transfer of assets, assumption of liabilities, or emission of equity instruments.

Business acquisition date – the date on which the acquirer assumes risks and rewards arising from the assets of another entity, and an obligation to meet liabilities of that other entity related to the acquired business.

Business combination – obtaining direct or indirect control over another entity (the bringing together of separate entities into one reporting entity), acquisition of a business and reorganisation of entities by way of merger by acquisition or by the formation of a new entity.

III. ACCOUNTING FOR BUSINESS COMBINATIONS

4. A business combination may be realised in different ways. Forms of business combinations:
   4.1. Obtaining control over another entity.
   4.2. Acquisition of entire or part of business of another entity.
   4.3. Reorganisation of entities by way of merger.

5. When the control over another entity is obtained, the date from which the acquirer gains control is the entity acquisition date (hereinafter, the acquisition date). In determining the acquisition date, the substance of the acquisition and the effective control over another entity, rather than formal requirements, have to be considered.

6. If a business is acquired, the date on which the acquirer assumes risks and rewards arising from the assets of another entity, and an obligation to meet liabilities of that other entity related to the acquired business, is the business acquisition date (hereinafter, the acquisition date).

7. An acquirer shall record a business combination in accounting and present it in financial statements as from the acquisition date.

8. Upon obtaining the control of another entity, the parent-subsidiary relations arise. At the end of the reporting period the acquirer shall prepare consolidated financial statements if it is required to prepare such statements by the legal acts.

9. All business combinations, except for those involving entities under common control, shall be accounted for by applying the purchase method. Business combinations involving entities
under common control are accounted for in accordance with the provisions of section VII of this Standard.

10. If one entity obtains control over another entity and in its separate financial statements it presents such investments in subsidiaries applying the cost method, it shall apply the purchase method only in its consolidated financial statements.

11. Under the purchase method an acquisition of a business is recorded in accounting in the manner similar to the purchase of other assets.

12. Acquisition of equity instruments (thereinafter, shares) of another entity may be achieved in several stages. If so, each exchange transaction shall be treated separately. On each acquisition date through a step-by-step comparison of the price of the individual investments with the value of the acquired interest in net assets of the acquiree, the cost of each acquisition is determined, and the goodwill (negative goodwill), that is presented in consolidated financial statements as intangible assets or losses (gains) from acquiring investments, is calculated.

13. When an acquisition of shares is achieved in stages, the fair values of assets and liabilities may vary at the date of each exchange transaction. If the fair values of all identifiable assets and liabilities relating to each acquisition of shares are restated, any value adjustment relating to the previously held interest in the net assets of the acquiree is accounted for as revaluation and is presented in consolidated financial statements as revaluation reserve (results) or a change in it. In this case valuation of assets and liabilities at fair value is not treated as a change in accounting policies.

14. Not every transaction may qualify as a business combination. Prior to qualifying a transaction as such, it may qualify as an ordinary investment or investment in an associate. Ordinary investments are recognised, accounted for and presented in financial statements in accordance with 15 Business Accounting Standard “Financial Assets and Financial Liabilities”, and investments in associates in accordance with 15 Business Accounting Standard “Investments in Associates”.

IV. REORGANISATION OF INDEPENDENT ENTITIES BY WAY OF MERGER

15. One or more independent entities may be reorganised by merging them with an entity that continues its operations after the reorganisation, or by transferring the assets and liabilities of two or more entities to a newly formed entity.

16. A merger of independent entities may be effected by:

16.1. merger by acquisition, whereby one or more entities transfer all their assets, liabilities, rights and obligations to another entity that continues in operation after the reorganisation, and cease to exist as legal persons;

16.2. merger by formation of a new entity, whereby a new entity is formed from two or more independent entities which cease to exist as legal persons after the reorganisation, and the new entity assumes assets, liabilities, rights and obligations of the reorganised entities.

17. The date from which assets, liabilities, rights and obligations of the reorganised entities are transferred to the entity continuing in operation after the reorganisation is the acquisition date.

18. The entity continuing in operation after the reorganisation shall record the acquisition in accounting on the acquisition date and present it in financial statements.

19. Reorganisation of independent entities by way of merger shall be accounted for by applying the purchase method.

20. Irrespective of the fact that as a result of a merger entities cease to exist when two or more independent entities are combined to form a new entity, one of the combining entities shall be identified as the acquirer. The acquirer is identified in view of indications provided in paragraph 26 of this Standard.
V. APPLICATION OF THE PURCHASE METHOD

21. When a control over another entity is obtained, application of the purchase method involves the following steps:
   21.1. identifying the acquirer;
   21.2. measuring the cost of acquiring the entity;
   21.3. measuring the assets and liabilities of the acquiree;
   21.4. measuring the difference between the price paid by the acquirer and the value of the acquired interest in the net assets of the acquiree, which is recognised as goodwill (negative goodwill) or losses (gains) from acquiring investments and presented in consolidated financial statements.

22. When a business is acquired, application of the purchase method involves the following steps:
   22.1. measuring the cost of acquiring the business;
   22.2. measuring the assets and liabilities attributed to the acquired business;
   22.3. measuring the difference between the price paid by the acquirer of the business and the value of net assets of the acquired business, which is recognised as goodwill (negative goodwill) or losses (gains) from acquiring businesses.

23. When entities are reorganised by way of merger, application of the purchase method involves the following steps:
   23.1. identifying the acquirer;
   23.2. measuring the cost of acquiring the entity;
   23.3. measuring the assets and liabilities of the acquiree;
   23.4. measuring the difference between the price paid by the acquirer and the value of the acquired interest in the net assets of the acquiree, which is recognised as goodwill (negative goodwill) or losses (gain) from reorganising.

24. An acquirer shall be identified for all business combinations.

25. Control, as a rule, is obtained upon acquisition of more than 50 per cent of the voting shares. However, an entity which acquires less than 50 cent of the voting shares may also become the acquirer, if as a result of such business combination it acquires:
   25.1. power over more than a half of the voting shares of another entity by virtue of an agreement with other shareholders thereof;
   25.2. power to control operations of another entity according to Articles of Association or an agreement;
   25.3. power to appoint or remove the majority of members of the board or any other management body of another entity;
   25.4. power to cast the majority of votes at the meetings of the board or any other management body of another entity.

26. If upon obtaining control over another entity or reorganisation of entities by way of merger it is difficult to determine which of the entities is the acquirer on the basis of the criteria specified above, the following indications shall be taken into consideration:
   26.1. If the values of merging entities are different, the entity with the higher value is likely to be the acquirer.
   26.2. If the business combination is effected through an exchange of shares for cash, the entity that pays (has to pay) cash is likely to be the acquirer.
   26.3. If as a result of the business combination the management of one of the combining entities can exert influence in appointing managers of the entity continuing in operation after the reorganisation, the first entity is likely to be the acquirer.

27. The cost of acquisition is calculated at the acquisition date as the amount of cash or cash equivalents paid (or payable) or the fair value of other transferred assets, assumed liabilities or issued shares plus any costs directly attributable to the acquisition.
28. When an acquisition of a business or shares involves more than one exchange transaction, the cost of the acquisition is the aggregate cost of the individual transactions (the sum of costs of acquisitions).

29. When an acquisition is achieved in stages, the distinction between the date of acquisition and the dates of the exchange is important:

29.1. If control is obtained or entities are reorganised by way of merger, the purchase method is applied from the acquisition date when the acquirer obtains control over the acquiree or the entity continuing in operation after the reorganisation assumes all assets, liabilities, rights and obligations of the combined entities.

29.2. If a business is acquired, the purchase method is applied from the acquisition date when the acquirer assumes risks and rewards arising from the assets of another entity, and an obligation to meet liabilities of that other entity related to the acquired business.

30. Assets transferred and liabilities assumed are measured at their fair values at the date of the exchange transaction. When the settlement of the purchase consideration is deferred, the cost of the acquisition shall be determined by discounting the amounts payable to their present value at the date of exchange, taking into account any premium or discount likely to be incurred in settlement.

31. In determining the cost of acquisition when the settlement requires a transfer of shares, marketable securities issued by the acquirer or by the entity continuing in operation after reorganisation are measured at their fair value at the date of exchange. If the published price of a quoted share at the date of exchange is an unreliable indicator, it is necessary to consider fluctuations in the published price during the period before and after the pronouncement of the terms for the acquisition. When the market is unreliable or no quotation exists, the fair value of shares issued by the acquirer is estimated by reference to their price on other markets. Independent valuations or a valuation technique based on reliable information arising from an active market may be used as an aid in determining the fair value of issued shares.

32. The amount of costs related to emission of shares is deducted from the share premium, and where share premium does not exist, these costs are deducted from retained earnings or added to loss incurred. General, administrative and other costs which cannot be directly attributed to acquisition are excluded from the cost of acquisition and recognised as expenses of the period in which they were incurred.

33. If a purchase agreement contains conditions upon occurrence of which the amount payable for the acquiree should be adjusted and the amount of adjustment can be reliably estimated at the acquisition date, the acquirer adjusts the cost of the acquisition by this amount on the acquisition date. If according to the mentioned agreement the amount of adjustment cannot be reliably estimated at the acquisition date, the cost of acquisition is not adjusted. Later, when it is possible to estimate the amount of adjustment, the cost of acquisition shall be adjusted by such amount and the respective adjustment shall also be made in the amount of goodwill (negative goodwill).

34. The acquirer shall recognise acquired assets and liabilities of another entity held by the latter at the acquisition date, only if:

34.1. it can be reasonably expected that the acquirer will obtain economic benefits from the assets in future periods;

34.2. their acquisition cost, i.e. the cost at which the assets and liabilities will be recorded in the acquirer’s accounting, can be reliably measured.

35. Acquired assets and liabilities shall be measured at their fair value at the acquisition date.

36. If only a part of voting shares of another entity is acquired but control over it is obtained, in the consolidated balance sheet a portion of the difference in the value of assets and liabilities arising from their measurement at fair value at the acquisition date is attributed to minority interest as well as to the acquirer.

37. Acquired assets and liabilities are measured as follows:

37.1. Intangible assets are measured at their market value. Where there is no evidence of the market value, they are measured at the carrying amount.
37.2. Land and buildings are measured at their market value.

37.3. Plant and equipment are measured at their market value. Where there is no evidence of the market value because of the specialised nature of the plant and equipment or because the items are rarely sold, except as a part of a continuing business, they are valued at their replacement cost.

37.4. Securities traded in regulated or active securities markets are measured at their market value based on the quoted price in the active market, i.e. on the basis of the closing price in the active market at the acquisition date.

37.5. Other securities are measured at the value which is determined in consideration of the price of previous transactions if the circumstances have not changed significantly; or the price at which the shares of similar (comparable) companies were traded; or the price estimated by an independent valuation or by applying a valuation technique based on reliable information arising from an active market.

37.6. Inventories are measured at net realisable value.

37.7. Amounts receivable are measured at net value determined as the acquisition cost less amounts that are not expected to be recovered and, where applicable, the costs of recovery.

37.8. Accounts and notes payable, non-current debts, liabilities, accruals and other claims payable are measured by discounting the payable amounts to their present values at appropriate current interest rates.

37.9. Provisions for terminating or reducing activities of the acquiree are measured in the manner established in paragraph 44 of this Standard.

38. If it is impossible to determine the market value of assets specified in subparagraphs 37.2 and 37.4, other ways of measuring the fair value shall be applied.

39. If after acquisition the acquiree obtains additional data, which helps to make a more accurate measurement of the fair value of acquired assets and liabilities, the acquirer shall adjust the recorded values of assets, liabilities and goodwill respectively. Such adjustment can be carried out before preparing the financial statements of the next financial year. In later periods the adjusted amount shall be recognized as income or expenses.

40. The acquirer may recognise assets and liabilities that have not been recognised in the acquiree’s financial statements because prior to the acquisition they did not meet the recognition criteria.

41. Liabilities arising from the acquirer’s intent or actions related to future losses or other costs that are likely to be incurred as a result of the acquisition, regardless of whether they are related to the acquirer or the acquiree, shall be recognised at the acquisition date. These are not the acquirer’s liabilities at the acquisition date, and therefore they are not attributable to the cost of acquisition.

42. In some cases the acquirer shall recognise liabilities that have been treated by the acquiree as contingent liabilities and have not been presented in its financial statements.

43. If the acquirer draws up the plans related to the acquisition and the liabilities are an inseparable part of those plans, provisions against costs specified in paragraph 44 of this Standard may be recognised.

44. At the date of acquisition the acquirer may recognise a provision, other than the liability of the acquiree, only if at the date of acquisition it has prepared a business plan approved by the management body of the entity which envisages termination or reduction of the entity’s business and which is related to:

44.1. compensation to the acquiree’s employees for termination of their employment contracts;

44.2. reduction of production capacities of the acquiree;

44.3. restriction of the range of products of the acquiree;

44.4. termination of the acquiree’s contracts which have started generating losses, because at the acquisition date or earlier the acquiree notified its counterparty about pending termination of the contract.
45. All provisions recognised according to paragraph 44 shall be intended exclusively for costs specified in subparagraphs 44.1, 44.2, 44.3 and 44.4.

VI. ACCOUNTING FOR GOODWILL (NEGATIVE GOODWILL) AND ITS PRESENTATION IN FINANCIAL STATEMENTS

46. A portion of the price paid by the acquirer of an entity or business that exceeds the value of net assets of the acquired entity or business is recognised as goodwill if the acquirer of the entity or business expects to obtain future economic benefits, or as losses from a business combination.

47. A portion of the value of net assets of the acquired entity or business that exceeds the price paid by the acquirer of the entity or business may be recognised as negative goodwill if it is not recognised as a gain from a business combination.

48. Before recognising negative goodwill the acquirer of an entity or business shall obtain evidence that the assets and liabilities of the acquired entity or business are measured accurately.

49. At the acquisition date goodwill (negative goodwill) is recognised at the acquisition cost.

50. Goodwill shall be amortised. Amortisation period of goodwill is always finite. It is recommended to establish the amortisation period of goodwill of 5 years but in exceptional cases a longer useful life of goodwill may be set.

51. Goodwill shall be amortised by applying the straight-line amortisation method. The amount of amortisation for each period shall be recognised as expenses.

52. Many factors shall be considered in estimating the amortisation period of goodwill including:
   52.1. the nature and expected useful life of the acquired business;
   52.2. the stability and expected period of existence of the industry where the acquired business operates;
   52.3. the effects of product obsolescence, changes in demand and other economic factors on the acquired business;
   52.4. whether key management personnel or employees are expected to continue working for the entity and whether the acquired business could be efficiently managed by another management team;
   52.5. the level of costs and funding required to obtain the expected future economic benefits from the acquired business and the company’s ability and intent to reach such level;
   52.6. expected actions by competitors or potential competitors;
   52.7. the period of control over the acquired business and legal, regulatory or contractual provisions affecting its useful life.

53. The amortisation period of goodwill shall be reviewed every year. It shall be checked whether the set amortisation period is not too long. If the expected amortisation period is significantly different from previous estimates, it shall be adjusted accordingly in the reporting period.

54. When an entity determines that the goodwill has impaired, it shall apply the same accounting principles as those applied in recording impairment losses of other assets. Amortisation is calculated on the newly estimated value of goodwill.

55. When the estimated amortisation period of goodwill exceeds 20 years, reviews shall be carried out on a yearly basis to determine likely impairments in value.

56. The portion of negative goodwill related to expected future losses and expenses that are identified in the acquisition plan and can be measured reliably, but are not recognised as liabilities at the acquisition date, shall be amortised systematically by reducing operating expenses in the income statement of the period when the expected future losses and expenses are incurred.

57. The portion of negative goodwill related or unrelated to expected future losses and expenses that cannot be measured reliably at the acquisition date, shall be amortised and recognised in the income statement as follows:
57.1. the amount of negative goodwill not exceeding the fair values of acquired non-current tangible and intangible assets shall be amortised systematically over the remaining useful life of the assets in proportion to the amounts of their depreciation or amortisation and presented in the income statement by reducing operating expenses;

57.2. the amount of negative goodwill exceeding the fair values of acquired non-current tangible and intangible assets shall be recognised as a gain from business combination immediately.

58. Goodwill (negative goodwill) is presented in the balance sheet at its book value that is determined by deducting amortisation and impairment from the acquisition cost.

59. Upon obtaining control over another entity, goodwill (negative goodwill) or losses (gains) from a business combination shall be presented only in consolidated financial statements. When control over another entity is obtained and the acquirer applies the equity method for investment accounting, in the acquirer’s balance sheet goodwill arising from such business combination is presented in the same line item as the investment into the acquiree. When control over another entity is obtained and the acquirer applies the cost method for investment accounting, goodwill arising from such business combination is not presented in the acquirer's balance sheet.

60. Goodwill (negative goodwill) arising from a business combination when the entire or part of business of another entity is acquired is presented in the intangible assets part of the acquirer's balance sheet.

61. Goodwill (negative goodwill) arising from a business combination when two or more entities are reorganised by way of merger is presented in the intangible assets part of the balance sheet of the entity continuing in operation after the reorganisation.

VII. BUSINESS COMBINATIONS INVOLVING ENTITIES UNDER COMMON CONTROL

62. A business combination of entities under common control is a combination in which all of the combining entities are ultimately controlled by the same person or persons both before and after the business combination.

63. If one of entities under common control obtains control over another entity under common control, such acquisition is treated as a business combination. For preparation of consolidated financial statements, either the purchase method may be applied, or the balance sheets of the entities may be combined without measuring the fair value of assets and liabilities, i.e. by adding the carrying amounts of the acquiree’s assets and liabilities to the carrying amounts of the acquirer’s assets and liabilities.

64. If one of entities under common control acquires the entire or part of business of another entity under common control, such acquisition is treated as a business combination. For accounting purposes either the purchase method may be applied, or the carrying amounts of assets and liabilities related to the acquired business may be added to the carrying amounts of the acquirer’s assets and liabilities.

65. If entities under common control are reorganised by way of merger, the purchase method shall not be applied. The balance sheets of the entities are combined without measuring the fair value of assets and liabilities by adding the carrying amounts of the acquiree’s assets and liabilities to the carrying amounts of the acquirer’s assets and liabilities.

VIII. BUSINESS COMBINATIONS INVOLVING A PARENT AND SUBSIDIARIES

66. Combining a parent and a subsidiary into one entity is a legal registration of a previous business combination, therefore it is not treated as a new business combination. The business combination took place when the control over the subsidiary was obtained.

67. Similarly to reorganisation of independent entities by way of merger, a reorganisation of a parent and subsidiaries by way of merger may be effected by:
67.1. merger by acquisition, whereby a subsidiary is combined with a parent, or a parent is combined with a subsidiary which continues in operation after the reorganisation and assumes all assets, liabilities, rights and obligations of the entity ceasing to exist after the reorganisation;
67.2. merger by formation of a new entity, whereby a new entity is formed from a parent and subsidiaries which cease to exist as a legal person after the reorganisation, and the new entity assumes assets, liabilities, rights and obligations of the reorganised entities.
68. Upon combining a parent and a subsidiary into one entity when one of them ceases to exist, consolidated financial statements which comprise only the data of the reorganised entities are prepared at the date of the business combination.
69. Consolidated financial statements of the combined entities prepared at the date of the business combination shall be the financial statements of the entity continuing in operation after reorganisation or of the new entity irrespectively of the name of the entity after the business combination.
70. Upon the merger the unamortised portion of goodwill (negative goodwill) recognised when the control over the subsidiary was obtained is presented in the intangible assets part of financial statements of the entity continuing in operation after the reorganisation or of the new entity.
71. If a parent acquires the entire or part of business of a subsidiary, or a subsidiary acquires the entire or part of business of a parent, such acquisition is treated as a business combination. For accounting purposes either the purchase method may be applied, or the carrying amounts of assets and liabilities related to the acquired business are added to the carrying amounts of assets and liabilities of the acquirer.

IX. DISCLOSING INFORMATION IN FINANCIAL STATEMENTS

72. Explanatory notes shall disclose the following information about business combinations:
72.1. the names and activities of the combining entities;
72.2. the effective date of the combination for accounting purposes;
72.3. operations terminated as a result of the business combination;
72.4. the number of acquired voting shares;
72.5. the cost of acquisition and the amount paid or payable.
73. Explanatory notes shall disclose the following information about goodwill:
73.1. the amortisation period of goodwill;
73.2. the line items of the income statement in which the amortisation of goodwill is included;
73.3. the amount of goodwill at the beginning and at the end of the reporting period;
73.4. all adjustments of goodwill resulting from the change in the value of assets or liabilities;
73.5. the amount of amortisation of goodwill and the amount recognised as expenses during the reporting period.
74. Explanatory notes shall disclose the following information about negative goodwill:
74.1. the amount of negative goodwill at the beginning and at the end of the reporting period;
74.2. the amortisation period of negative goodwill;
74.3. the line items of the income statement in which negative goodwill is recognised as income or reduces expenses;
74.4. all additional negative goodwill recognised during the reporting period;
74.5 all adjustments of negative goodwill resulting from the change in the value of assets or liabilities;
74.6. the amount of amortisation of negative goodwill and the amount recognised as income during the reporting period.
75. In explanatory notes provisions formed for reducing or terminating operations of the entity shall be disclosed separately for each business combination.
X. FINAL PROVISIONS

76. The revised version of this Standard shall be effective for financial statements covering periods beginning on or after 1 January 2008. The revised version may be applied in preparing financial statements for the earlier reporting periods.