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IPSAS®

IPSAS ® Accounting Standard

Definition of an Operation and Recognition of Acquired Liabilities and Contingent Liabilities (Amendments to IPSAS 40)

IPSASB International Public Sector Accounting Standards Board®

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DEFINITION OF AN OPERATION AND RECOGNITION OF ACQUIRED LIABILITIES AND CONTINGENT LIABILITIES (AMENDMENTS TO IPSAS 40)

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Objective

1. The objective of *Definition of an Operation and Recognition of Acquired Liabilities and Contingent Liabilities* (Amendments to IPSAS 40) is to make amendments to IPSAS 40, *Public Sector Combinations*, to align with amendments to IFRS 3 *Business Combinations* arising from *Definition of a Business* (Amendments to IFRS 3) and *Reference to the Conceptual Framework* (Amendments to IFRS 3) issued by the International Accounting Standards Board (IASB®)[1].

IFRS Alignment Amendments to IPSAS 40:

IASB's Publication	***Equivalent IPSAS Standard***	***Summary of Change***
Definition of a Business (Amendments to IFRS 3) (Issued October 2018)	IPSAS 40, *Public Sector Combinations*	The amendments include: • Addition of related application guidance and illustrative examples regarding the definition of "operation"; and • Addition of an optional concentration test to simplify the assessment of whether an acquired set of activities and assets is an operation. (See **Part 1**)
References to the Conceptual Framework (Amendments to IFRS 3) (Issued May 2020)	IPSAS 40, *Public Sector Combinations*	The amendments include: • Reference to guidance in IPSAS 19, *Provisions, Contingent Liabilities and Contingent Assets* to determine whether a present obligation exists on acquisition date as a result of past events; • Clarification that only contingent liabilities which are present obligations in accordance with IPSAS 19, and whose fair value can be measured reliably, can be recognized; and • An explicit prohibition against the recognition of contingent assets to be consistent with IPSAS 19. (See **Part 2**)

[1] IPSAS Standards do not duplicate the Basis for Conclusions developed by the IASB. The Basis for Conclusions included in IPSAS Standards includes consideration taken into account and conclusions drawn by the IPSASB when developing the pronouncement.

Amendment: Part 1 – Definition of an Operation

Paragraphs 6, AG4–AG6, AG8 and AG9 are amended. Paragraphs 126J, AG4A–AG4C, AG5A and AG9A–AG9D, headings above paragraphs AG4A, AG5 and AG9, pargraph BC95, paragraph IG3, heading above paragraph IG3, diagram below paragraph IG3, and paragraphs IE279–IE326 and their related headings are added. Paragraph AG7 is deleted. New text is underlined and deleted text is struck through.

Definitions

…

6. **An entity shall determine whether a transaction or other event is a public sector combination by applying the definitions in this Standard, which requires that the assets and liabilities constitute an operation. If the assets and liabilities do not constitute an operation, the entity shall account for the transaction or other event in accordance with other IPSAS. Paragraphs AG2–AG9D provide guidance on identifying a public sector combination.**

…

Effective Date

126J. Paragraphs 6, AG4–AG6, AG8 and AG9 were amended, paragraphs AG4A–AG4C, AG5A and AG9A–AG9D were added, and paragraph AG7 was deleted by *Definition of an Operation and Recognition of Acquired Liabilities and Contingent Liabilities* (Amendments to IPSAS 40), issued in October 2026. An entity shall apply these amendments to public sector combinations for which the amalgamation date or acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2028, and to asset acquisitions that occur on or after the beginning of that period. Earlier application of these amendments is permitted. If an entity applies these amendments for an earlier period, it shall disclose that fact.

Appendix A

Application Guidance

This Appendix is an integral part of IPSAS 40.

Definitions (see paragraph 5)

…

AG4. An operation consists of inputs and processes applied to those inputs that have the ability to ~~create~~ contribute to the creation of outputs. ~~Although operations usually have outputs, outputs are not required for an integrated set of activities and related assets and/or liabilities to qualify as an operation.~~ For the purposes of this standard, the three elements of an operation are defined as follows (see paragraphs AG3–AG9D for guidance on the elements of an operation):

(a) **Input:** Any economic resource that creates outputs, or has the ability to ~~create,~~ contribute to the creation of outputs when one or more processes are applied to it.

(b) **Process:** Any system, standard, protocol, convention or rule that when applied to an input or inputs, creates outputs or has the ability to ~~create~~ contribute to the creation of outputs.

(c) **Output:** The result of inputs and processes applied to those inputs that provide, or have the ability to provide, goods and/or services.

The definitions of an input and an output differ from those in RPG 3, *Reporting Service Performance Information*. This is because RPG 3 focuses on recipients who are external to the entity; an operation may have recipients who are internal to an entity.

Optional Test to Identify Concentration of Fair Value

AG4A. Paragraph AG4B sets out an optional test (the concentration test) to permit a simplified assessment of whether a set of activities and assets acquired in an acquisition is not an operation. An entity may elect to apply, or not apply, the test. An entity may make such an election separately for each transaction or other event. The concentration test has the following consequences:

(a) If the concentration test is met, the set of activities and assets is determined not to be an operation and no further assessment is needed.

(b) If the concentration test is not met, or if the entity elects not to apply the test, the entity shall then perform the assessment set out in paragraphs AG5–AG9D.

AG4B. The concentration test is met 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. For the concentration test:

(a) Gross assets acquired shall exclude cash and cash equivalents, deferred tax assets (if applicable), and goodwill resulting from the effects of deferred tax liabilities (if applicable).

(b) The fair value of the gross assets acquired shall include any consideration transferred (plus the fair value of any non-controlling interest and the fair value of any previously held interest) in excess of the fair value of net identifiable assets acquired. The fair value of the gross assets acquired may normally be determined as the total obtained by adding the fair value of the consideration transferred (plus the fair value of any non-controlling interest and the fair value of any previously held interest) to the fair value of the liabilities assumed (other than deferred tax liabilities, if applicable), and then excluding the items identified in subparagraph (a). However, if the fair value of the gross assets acquired is more than that total, a more precise calculation may sometimes be needed.

(c) A single identifiable asset shall include any asset or group of assets that would be recognized and measured as a single identifiable asset in a public sector combination.

(d) If a tangible asset is attached to, and cannot be physically removed and used separately from, another tangible asset (or from an underlying asset subject to a lease, as defined in IPSAS 43, *Leases*), without incurring significant cost, or significant diminution in utility or fair value to either asset (for example, land and buildings), those assets shall be considered a single identifiable asset.

(e) When assessing whether assets are similar, an entity shall consider the nature of each single identifiable asset and the risks associated with managing and creating outputs from the assets (that is, the risk characteristics).

(f) The following shall not be considered similar assets:

(i) A tangible asset and an intangible asset;

(ii) Tangible assets in different classes (for example, inventory, infrastructure, vehicles, and tangible natural resources held for conservation) unless they are considered a single identifiable asset in accordance with the criterion in subparagraph (d);

(iii) Identifiable intangible assets in different classes (for example, brand names, licenses and intangible assets under development);

(iv) A financial asset and a non-financial asset;

(v) Financial assets in different classes (for example, accounts receivable and investments in equity instruments); and

(vi) Identifiable assets that are within the same class of asset but have significantly different risk characteristics.

AG4C. The requirements in paragraph AG4B do not modify the guidance on similar assets in IPSAS 31, *Intangible Assets*; nor do they modify the meaning of the term 'class' in IPSAS 45, *Property, Plant, and Equipment*, IPSAS 31, and IPSAS 30, *Financial Instruments: Disclosures*.

Elements of an Operation

AG5. Although operations usually have outputs, outputs are not required for an integrated set of activities and assets to qualify as an operation. To be capable of being conducted and managed for the ~~purposes defined,~~ purpose identified in the definition of an operation, an integrated set of activities and assets and/or liabilities requires two essential elements—inputs and processes applied to those inputs~~, which together are or will be used to create outputs~~. ~~However, a~~An operation need not include all of the inputs or processes that the transferor used in operating that operation ~~if the entity that receives the operation or operations is capable of continuing to produce outputs, for example, by integrating the operation with their own inputs and processes~~. However, to be considered an operation, an integrated set of activities and assets must include, at a minimum, an input and a substantive process that together contribute to the ability to create output. Paragraphs AG9–AG9D specify how to assess whether a process is substantive.

AG5A. If a set of activities and assets has outputs, continuation of revenue does not on its own indicate that both an input and a substantive process have been acquired or received.

AG6. The nature of the elements of an operation varies by sector and by the structure of an entity's operations (activities), including the entity's stage of development. Established operations often have many different types of inputs, processes and outputs, whereas new operations often have few inputs and processes and sometimes only a single output (product). Nearly all operations also have liabilities, but an operation need not have liabilities. Furthermore, a set of activities and assets that is not an operation might have liabilities.

~~AG7. An integrated set of activities and assets and/or liabilities in the development stage might not have outputs. In these cases, the entity that receives the operation should consider other factors to determine whether the set is an operation. Those factors include, but are not limited to, whether the set:~~

~~(a) Has begun planned principal activities;~~

~~(b) Has employees, intellectual property and other inputs and processes that could be applied to those inputs;~~

~~(c) Is pursuing a plan to produce outputs; and~~

~~(d) Will be able to obtain access to service recipients that will receive the outputs.~~

~~Not all of those factors need to be present for a particular integrated set of activities and assets and/or liabilities in the development stage to qualify as an operation.~~

AG8. Determining whether a particular set of activities and assets and/or liabilities is an operation ~~should~~ shall be based on whether the integrated set is capable of being conducted and managed as an operation by another entity. Thus, in evaluating whether a particular set is an operation, it is not relevant whether a transferor operated the set as an operation or whether the acquirer intends to operate the set as an operation.

Assessing Whether a Process is Substantive

AG9. ~~In the absence of evidence to the contrary, a particular set of activities and assets and/or liabilities in which goodwill is present shall be presumed to be an operation. However, an operation need not have goodwill~~. Paragraphs AG9A–AG9D explain how to assess whether a process is substantive if the set of activities and assets does not have outputs (paragraph AG9B) and if it does have outputs (paragraph AG9C).

AG9A. An example of a set of activities and assets that does not have outputs at the transaction date is an early-stage entity that has not started generating revenue. (Such early-stage entities do not include organizations which do not have a profit-making objective and are not expected to generate revenue from their operations.) Moreover, if a set of activities and assets was generating revenue at the transaction date, it is considered to have outputs at that date, even if subsequently it will no longer generate revenue from external customers, for example because it will be integrated by the acquirer or resulting entity.

AG9B. If a set of activities and assets does not have outputs at the transaction date, a process (or group of processes) shall be considered substantive only if:

(a) It is critical to the ability to develop or convert an input or inputs into outputs; and

(b) The inputs include both an organized workforce that has the necessary skills, knowledge, or experience to perform that process (or group of processes) and other inputs that the organized workforce could develop or convert into outputs. Those other inputs could include:

(i) Intellectual property that could be used to develop a good or service;

(ii) Other economic resources that could be developed to create outputs; or

(iii) Rights to obtain access to necessary materials or rights that enable the creation of future outputs.

Examples of the inputs mentioned in subparagraphs (b)(i)–(iii) include technology, in-process research and development projects, and mineral interests.

AG9C. If a set of activities and assets has outputs at the transaction date, a process (or group of processes) shall be considered substantive if, when applied to an input or inputs, it:

(a) Is critical to the ability to continue producing outputs, and the inputs include an organized workforce with the necessary skills, knowledge, or experience to perform that process (or group of processes); or

(b) Significantly contributes to the ability to continue producing outputs and:

(i) Is considered unique or scarce; or

(ii) Cannot be replaced without significant cost, effort, or delay in the ability to continue producing outputs.

AG9D. The following additional discussion supports both paragraphs AG9B and AG9C:

(a) A binding arrangement (including a contract) is an input and not a substantive process. Nevertheless, a contract, for example, a contract for outsourced property management or outsourced asset management, may give access to an organized workforce. An entity shall assess whether an organized workforce accessed through such a contract performs a substantive process that the entity controls. Factors to be considered in making that assessment include the duration of the contract and its renewal terms.

(b) Difficulties in replacing an organized workforce may indicate that the organized workforce performs a process that is critical to the ability to create outputs.

(c) A process (or group of processes) is not critical if, for example, it is ancillary or minor within the context of all the processes required to create outputs.

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, IPSAS 40.

…

Revisions of IPSAS 40 as a result of *Definition of an Operation and Recognition of Acquired Liabilities and Contingent Liabilities* (Amendments to IPSAS 40)

BC95. The IPSASB reviewed the revisions to IFRS 3 included in the narrow scope amendments titled *Definition of a Business* (Amendments to IFRS 3) issued by the IASB in October 2018, the IASB's rationale for making these amendments as set out in its Basis for Conclusions and generally concurred that there was no public sector specific reason for not adopting the amendments.

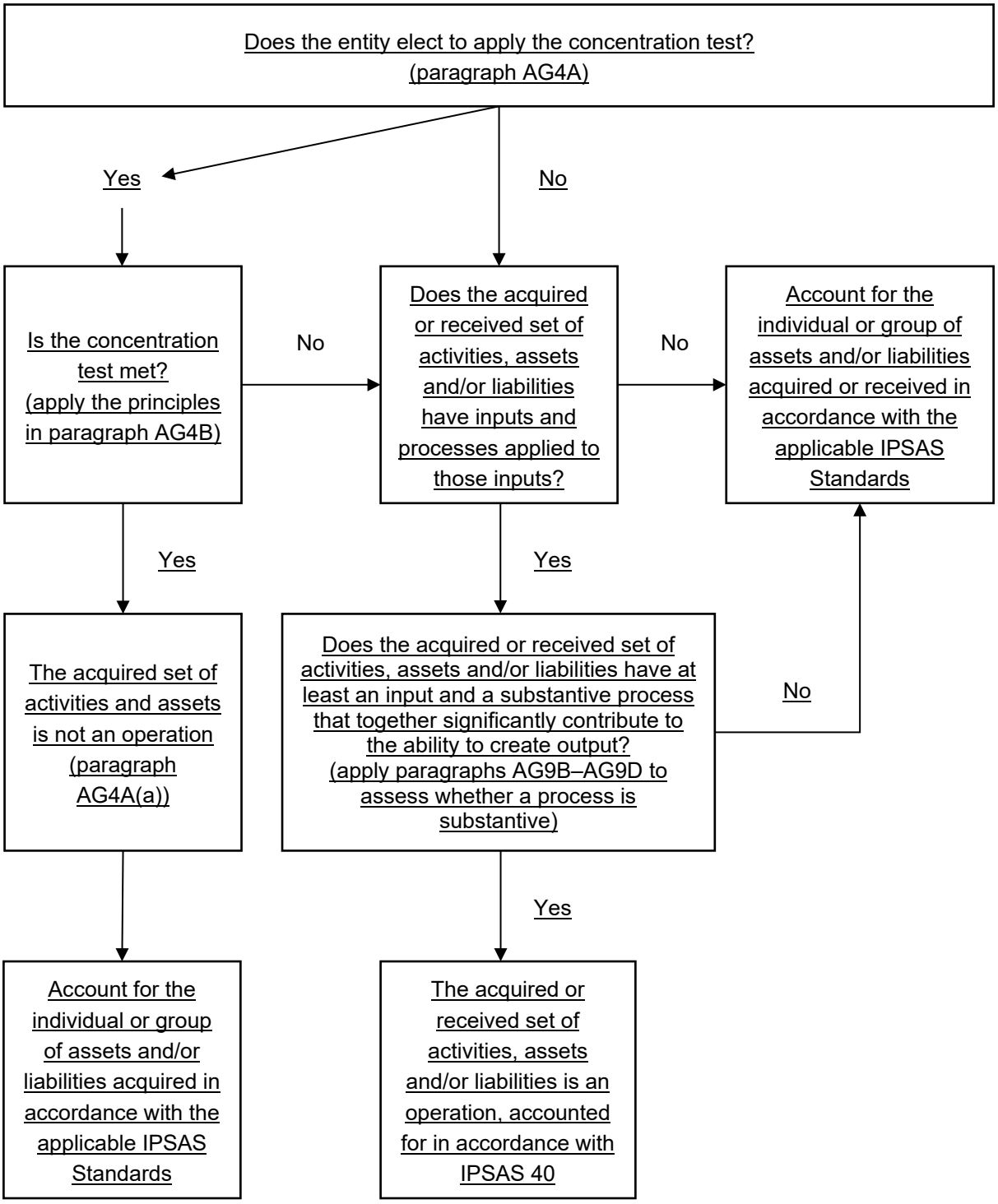
Implementation Guidance

This guidance accompanies, but is not part of, IPSAS 40.

…

Optional Test to Identify Concentration of Fair Value

IG3. The diagram below summarizes the process established by IPSAS 40 for assessing whether a set of activities and assets and/or liabilities is an operation, including when an entity elects, or does not elect, to apply the optional concentration test set out in paragraphs AG4A–AG9D.



Amendments to the Illustrative Examples accompanying IPSAS 40, *Public Sector Combinations*

Illustrative Examples

These examples accompany, but are not part of, IPSAS 40.

…

Definition of an Operation

IE279. The examples in paragraphs IE280–IE326 illustrate application of the guidance in paragraphs AG4–AG9D on the definition of an operation.

Example A—Acquisition of Real Estate

Scenario 1—Background

IE280. An entity (Purchaser) purchases a portfolio of 10 single-family homes as part of a social housing program that each has an in-place lease. The fair value of the consideration paid is equal to the aggregate fair value of the 10 single-family homes acquired. Each single-family home includes the land, building and property improvements. Each home has a different floor area and interior design. The 10 single-family homes are located in the same area and the classes of customers (e.g., tenants) are similar. The risks associated with operating in the real estate market of the homes acquired are not significantly different. No employees, other assets, processes or other activities are transferred.

Scenario 1—Application of Requirements

IE281. Purchaser elects to apply the optional concentration test set out in paragraph AG4B and concludes that:

(a) Each single-family home is considered a single identifiable asset in accordance with paragraph AG4B for the following reasons:

(i) The building and property improvements are attached to the land and cannot be removed without incurring significant cost; and

(ii) The building and the in-place lease are considered a single identifiable asset, because they would be recognized and measured as a single identifiable asset in a public sector combination (see paragraph AG89).

(b) The group of 10 single-family homes is a group of similar identifiable assets because the assets (all single-family homes) are similar in nature and the risks associated with managing and creating outputs are not significantly different. This is because the types of homes and classes of customers are not significantly different.

(c) Consequently, substantially all of the fair value of the gross assets acquired is concentrated in a group of similar identifiable assets.

IE282. Therefore, Purchaser concludes that the acquired set of activities and assets is not an operation.

Scenario 2—Background

IE283. Assume the same facts as in Scenario 1 except that Purchaser also purchases a multi-tenant corporate office park with six 10-storey office buildings that are fully leased. The additional set of activities and assets acquired includes the land, buildings, leases and contracts for outsourced cleaning, security and maintenance. No employees, other assets, other processes or other activities are transferred. The aggregate fair value associated with the office park is similar to the aggregate fair value associated with the 10 single-family

homes. The processes performed through the contracts for outsourced cleaning and security are ancillary or minor within the context of all the processes required to create outputs.

Scenario 2—Application of Requirements

IE284. Purchaser elects to apply the optional concentration test set out in paragraph AG4B and concludes that the single-family homes and the office park are not similar identifiable assets, because the single-family homes and the office park differ significantly in the risks associated with operating the assets, obtaining tenants and managing tenants. In particular, the scale of operations and risks associated with the two classes of customers are significantly different. Consequently, the fair value of the gross assets acquired is not substantially all concentrated in a group of similar identifiable assets, because the fair value of the office park is similar to the aggregate fair value of the 10 single-family homes. Thus, Purchaser assesses whether the set meets the minimum requirements to be considered an operation in accordance with paragraphs AG5–AG9D.

IE285. The set of activities and assets has outputs because it generates revenue through the in-place leases. Consequently, Purchaser applies the criteria in paragraph AG9C to determine whether any processes acquired are substantive.

IE286. Purchaser concludes that the criterion in paragraph AG9C(a) is not met because:

(a) The set does not include an organized workforce; and

(b) Purchaser considers that the processes performed by the outsourced cleaning, security and maintenance personnel (the only processes acquired) are ancillary or minor within the context of all the processes required to create outputs (see paragraph AG9D(c)) and, therefore, are not critical to the ability to continue producing outputs.

IE287. After considering the only processes acquired, those performed by the outsourced cleaning, security and maintenance personnel, Purchaser also concludes that the criteria in paragraph AG9C(b) are not met. Either of the following reasons justifies that conclusion:

(a) The processes do not significantly contribute to the ability to continue producing outputs.

(b) The processes are readily accessible in the marketplace. Thus, they are not unique or scarce. In addition, they could be replaced without significant cost, effort, or delay in the ability to continue producing outputs.

IE288. Because none of the criteria in paragraph AG9C are met, Purchaser concludes that the acquired set of activities and assets is not an operation.

Scenario 3—Background

IE289. Assume the same facts as in Scenario 2, except that the acquired set of activities and assets also includes the employees responsible for leasing, tenant management, and managing and supervising all operational processes.

Scenario 3—Application of Requirements

IE290. Purchaser elects not to apply the optional concentration test set out in paragraph AG4B and therefore assesses whether the set meets the minimum requirements to be considered an operation in accordance with paragraphs AG5–AG9D.

IE291. The acquired set of activities and assets has outputs because it generates revenue through the in-place leases. Consequently, Purchaser applies the criteria in paragraph AG9C.

IE292. Purchaser concludes that the criterion in paragraph AG9C(a) is met because the set includes an organized workforce with the necessary skills, knowledge or experience to perform processes (i.e., leasing, tenant management, and managing and supervising the operational processes) that are substantive because they are critical to the ability to continue producing outputs when applied to the acquired inputs (i.e., the land, buildings and in-place leases). Furthermore, Purchaser concludes that the criterion in paragraph AG5 is met because those substantive processes and inputs together significantly contribute to the ability to create output. Consequently, Purchaser concludes that the acquired set of activities and assets is an operation.

Example B—Acquisition of a Drug Candidate

Scenario 1—Background

IE293. An entity (Purchaser) purchases a legal entity that contains:

(a) The rights to an in-process research and development project that is developing a compound to treat diabetes and is in its final testing phase (Project 1). Project 1 includes the historical know-how, formula protocols, designs and procedures expected to be needed to complete the final testing phase.

(b) A contract that provides outsourced clinical trials. The contract is priced at current market rates and a number of vendors in the marketplace could provide the same services. Therefore, the fair value associated with this contract is nil. Purchaser has no option to renew the contract.

No employees, other assets, other processes or other activities are transferred.

Scenario 1—Application of Requirements

IE294. Purchaser elects to apply the optional concentration test set out in paragraph AG4B and concludes that:

(a) Project 1 is a single identifiable asset because it would be recognized and measured as a single identifiable intangible asset in a public sector combination.

(b) Because the acquired contract has a fair value of nil, substantially all of the fair value of the gross assets acquired is concentrated in Project 1.

IE295. Consequently, Purchaser concludes that the acquired set of activities and assets is not an operation.

Scenario 2—Background

IE296. Assume the same facts as in Scenario 1 except that the acquired set of activities and assets also includes another in-process research and development project that is developing a compound to treat Alzheimer's disease and is in its final testing phase (Project 2). Project 2 includes the historical know-how, formula protocols, designs, and procedures expected to be needed to complete the final phase of testing. The fair value associated with Project 2 is similar to the fair value associated with Project 1. No employees, other assets, processes or other activities are transferred.

Scenario 2—Application of Requirements

IE297. Purchaser elects to apply the optional concentration test set out in paragraph AG4B and concludes that:

(a) Project 1 and Project 2 are identifiable intangible assets that would each be recognized and measured as a separate identifiable asset in a public sector combination.

(b) Project 1 and Project 2 are not similar identifiable assets because significantly different risks are associated with managing and creating outputs from each asset. Each project has significantly different risks associated with developing, completing and marketing the compound to customers. The compounds are intended to treat significantly different medical conditions, and each project has a significantly different potential customer base.

(c) Consequently, the fair value of the gross assets acquired is not substantially all concentrated in a single identifiable asset or group of similar identifiable assets. Therefore, Purchaser assesses whether the set meets the minimum requirements to be considered an operation in accordance with paragraphs AG5–AG9D.

IE298. The acquired set of activities and assets does not have outputs because it has not started generating revenue. Thus, Purchaser applies the criteria in paragraph AG9B. Purchaser concludes that those criteria are not met for the following reasons:

(a) The set does not include an organized workforce; and

(b) Although the contract that provides outsourced clinical trials might give access to an organized workforce that has the necessary skills, knowledge or experience to perform processes needed to carry out the clinical trials, that organized workforce cannot develop or convert the inputs acquired by Purchaser into outputs. Successful clinical trials are a pre-condition for producing output, but carrying out those trials will not develop or convert the acquired inputs into outputs.

Consequently, Purchaser concludes that the acquired set of activities and assets is not an operation.

Example C—Acquisition of a Biotech Entity

Background

IE299. An entity (Purchaser) purchases a legal entity (Entity Biotech). Entity Biotech's operations include: research and development activities on several drug compounds that it is developing (in-process research and development projects); senior management and scientists who have the necessary skills, knowledge, or experience to perform research and development activities; and tangible assets (including a corporate headquarters, a research lab, and lab equipment). Entity Biotech does not yet have a marketable product and has not yet generated revenue. Each of the assets acquired has a similar fair value.

Application of Requirements

IE300. It is evident that the fair value of the gross assets acquired is not substantially all concentrated in a single identifiable asset or group of similar identifiable assets. Thus, the optional concentration test set out in paragraph AG4B would not be met. Consequently, Purchaser assesses whether the set meets the minimum requirements to be considered an operation in accordance with paragraphs AG5–AG9D.

IE301. Purchaser first assesses whether it has acquired any processes. No process is documented. Nevertheless, the acquired organized workforce has proprietary knowledge of Biotech's ongoing projects and experience with them. Applying paragraph AG4(b), Purchaser concludes that the intellectual capacity of the acquired organized workforce having the necessary skills and experience following rules and conventions provides the necessary processes that are capable of being applied to inputs to create outputs.

IE302. Purchaser next assesses whether the acquired processes are substantive. The set of activities and assets does not have outputs. Thus, Purchaser applies the criteria in paragraph AG9B. Purchaser concludes that those criteria are met because:

(a) The acquired processes are critical to the ability to develop or convert the acquired inputs into outputs; and

(b) The inputs acquired include both:

(i) An organized workforce that has the necessary skills, knowledge, or experience to perform the acquired processes; and

(ii) Other inputs that the organized workforce could develop or convert into outputs. Those inputs include the in-process research and development projects.

IE303. Finally, applying the criteria in paragraph AG5, Purchaser concludes that the acquired substantive processes and the acquired inputs together significantly contribute to the ability to create output. Consequently, Purchaser concludes that the acquired set of activities and assets is an operation.

Example D—Acquisition of a Television Station

Background

IE304. An entity (Seller) was winding down its operations in broadcasting and decided to sell its broadcasting assets to a government entity. The entity (Purchaser) purchases broadcasting assets from Seller. The acquired set of activities and assets includes only the communications license, the broadcasting equipment and an office building. Each of the assets acquired has a similar fair value. Purchaser does not purchase the processes needed to broadcast programs and it does not acquire any employees, other assets, other processes or other activities. Before the acquisition date, Seller stopped broadcasting using the set of activities and assets acquired by Purchaser.

Application of Requirements

IE305. Purchaser elects to apply the optional concentration test set out in paragraph AG4B and concludes that:

(a) The broadcasting equipment and building are not a single identifiable asset because the equipment is not attached to the building and can be removed without significant cost or diminution in utility or fair value of either asset.

(b) The license is an intangible asset, whereas the broadcasting equipment and building are tangible assets in different classes. Consequently, in accordance with paragraph AG4B(f), the assets are not considered similar to each other.

(c) Each of the single identifiable assets has similar fair value. Thus, the fair value of the gross assets acquired is not substantially all concentrated in a single identifiable asset or group of similar identifiable assets.

Consequently, Purchaser assesses whether the set of activities and assets meets the minimum requirements to be considered an operation in accordance with paragraphs AG5–AG9D.

IE306. The set of activities and assets does not have outputs, because Seller has already stopped broadcasting before the sale of the assets. Thus, Purchaser applies the criteria in paragraph AG9B. The set does not include an organized workforce, so it does not meet those criteria. Consequently, Purchaser concludes that the acquired set of activities and assets is not an operation.

Example E—Acquisition of a Closed Manufacturing Facility

Background

IE307. An entity (Purchaser) purchases a closed waste management facility—the land and the building—as well as the related equipment. The fair value of the equipment and the fair value of the facility are similar. To comply with local laws, Purchaser must take over the employees who worked in the facility. No other assets, processes or other activities are transferred. The acquired set of activities and assets stopped processing waste before the acquisition date.

Application of Requirements

IE308. Purchaser elects to apply the optional concentration test set out in paragraph AG4B and concludes that:

(a) The equipment and the facility are not a single identifiable asset because the equipment could be removed from the facility without significant cost or diminution in utility or fair value of either the equipment or the facility—the equipment is not attached to the facility and can be used in many other types of manufacturing facilities.

(b) The equipment and facility are not similar identifiable assets because they are in different classes of tangible assets.

(c) The fair values of the equipment and the facility are similar. Therefore, the fair value of the gross assets acquired is not substantially all concentrated in a single identifiable asset or group of similar identifiable assets.

Consequently, Purchaser assesses whether the set of activities and assets meets the minimum requirements to be considered an operation in accordance with paragraphs AG5–AG9D.

IE309. The acquired set of activities and assets does not have outputs at the acquisition date because it stopped producing outputs before then. Consequently, Purchaser applies the criteria in paragraph AG9B. The set includes an organized workforce that has the necessary skills, knowledge or experience to use the equipment, but it does not include another acquired input (such as intellectual property or inventories) that the organized workforce could develop or convert into outputs. The facility and the equipment cannot be developed or converted into outputs. Consequently, Purchaser concludes that the acquired set of activities and assets is not an operation.

Example F—License of Distribution Rights

Background

IE310. An entity (Purchaser) purchases from another entity (Seller) the exclusive sublicense to distribute Product X in a specified jurisdiction. Seller has the license to distribute Product X worldwide. As part of this transaction, Purchaser also purchases the existing customer contracts in the jurisdiction and takes over a supply contract to purchase Product X from the producer at market rates. None of the identifiable assets acquired have a fair value that constitutes substantially all of the fair value of the gross assets acquired. No employees, other assets, processes, distribution capabilities or other activities are transferred.

Application of Requirements

IE311. Purchaser elects to apply the optional concentration test set out in paragraph AG4B and concludes that:

(a) The identifiable assets that could be recognized in a public sector combination include the sublicense to distribute Product X, customer contracts and the supply contract;

(b) The sublicense and customer contracts are in different classes of intangible assets, so they are not similar identifiable assets; and

(c) Consequently, the fair value of the gross assets acquired is not substantially all concentrated in a single identifiable asset or group of similar identifiable assets.

Consequently, Purchaser assesses whether the set of activities and assets meets the minimum requirements to be considered an operation in accordance with paragraphs AG5–AG9D.

IE312. The set of activities and assets has outputs because at the acquisition date the license was generating revenue from customers in the jurisdiction specified in the sublicense. Consequently, Purchaser applies the criteria in paragraph AG9C. As explained in paragraph AG9D(a), acquired contracts are an input and not a substantive process. Purchaser considers next whether the acquired supply contract provides access to an organized workforce that performs a substantive process. Because the supply contract is not providing a service that applies a process to another acquired input, Purchaser concludes that the substance of the

supply contract is only that of buying Product X, without acquiring the organized workforce, processes and other inputs needed to produce Product X. Furthermore, the acquired sublicense is an input, not a process. Purchaser concludes that the set is not an operation because it does not include an organized workforce and Purchaser has acquired no substantive process that could meet the criteria in paragraph AG9C.

Example G—Acquisition of Loan Portfolio

Scenario 1—Background

IE313. A government (Purchaser) purchases a loan portfolio from an entity in financial difficulty (Seller) as part of a government assistance program. The portfolio consists of residential mortgage loans with terms, sizes and risk ratings that are not significantly different. No employees, other assets, processes or other activities are transferred.

Scenario 1—Application of Requirements

IE314. Purchaser elects to apply the optional concentration test set out in paragraph AG4B and concludes that:

(a) The assets (residential mortgage loans) are similar in nature;

(b) The risks associated with managing and creating outputs are not significantly different because the terms, sizes and risk ratings of the loans are not significantly different;

(c) The acquired loans are similar assets; and

(d) Consequently, substantially all of the fair value of the gross assets acquired is concentrated in a group of similar identifiable assets.

Consequently, Purchaser concludes that the acquired set of activities and assets is not an operation.

Scenario 2—Background

IE315. Assume the same facts as in Scenario 1 except that the portfolio of loans consists of commercial loans with terms, sizes and risk ratings that are significantly different. None of the acquired loans, and no group of loans with similar terms, sizes and risk ratings, have a fair value that constitutes substantially all of the fair value of the acquired portfolio. No employees, other assets, processes or other activities are transferred.

Scenario 2—Application of Requirements

IE316. Purchaser elects to apply the optional concentration test set out in paragraph AG4B and concludes that:

(a) The assets (commercial loans) are similar in nature;

(b) The risks associated with managing and creating outputs from the loans are significantly different because the terms, sizes and risk ratings of the loans are significantly different;

(c) The acquired loans are not similar identifiable assets; and

(d) Consequently, the fair value of the gross assets acquired is not substantially all concentrated in a group of similar identifiable assets.

Consequently, Purchaser assesses whether the set meets the minimum requirements to be considered an operation in accordance with paragraphs AG5–AG9D.

IE317. The portfolio of loans has outputs because it generates interest income. Consequently, Purchaser applies the criteria in paragraph AG9C. Acquired contracts are not a substantive process, as explained in paragraph AG9D(a). Moreover, the acquired set of activities and assets does not include an organized workforce and there are no acquired processes that could meet the criteria in paragraph AG9C(b). Consequently, Purchaser concludes that the acquired set of activities and assets is not an operation.

Scenario 3—Background

IE318. Assume the same facts as in Scenario 2 but Purchaser also takes over the employees of Seller (such as brokers, vendors, and risk managers) who managed the credit risk of the portfolio and the relationship with the borrowers. The consideration transferred to Seller is significantly higher than the fair value of the acquired portfolio of loans.

Scenario 3—Application of Requirements

IE319. As noted in paragraph IE316, the fair value of the gross assets acquired is not substantially all concentrated in a group of similar identifiable assets. Thus, the optional concentration test set out in paragraph AG4B would not be met. Consequently, Purchaser assesses whether the set meets the minimum requirements to be considered an operation in accordance with paragraphs AG5–AG9D.

IE320. The portfolio of loans has outputs because it generates interest income. Consequently, Purchaser applies the criteria in paragraph AG9C and concludes that the criterion in paragraph AG9C(a) is met because the set includes an organized workforce with the necessary skills, knowledge or experience to perform processes (customer relationship management and credit risk management) critical to the ability to continue producing outputs. Furthermore, Purchaser concludes that the criterion in paragraph AG5 is met because those substantive processes and the acquired inputs (the portfolio of loans) together significantly contribute to the ability to create output. Consequently, Purchaser concludes that the acquired set is an operation.

Example H—Determining the Fair Value of the Gross Assets Acquired

Background

IE321. An entity (Purchaser) holds a 20% interest in another entity (Entity A). At a subsequent date (the acquisition date), Purchaser acquires a further 50% interest in Entity A and obtains control of it. Entity A's assets and liabilities on the acquisition date are the following:

(a) A building with a fair value of CU500;

(b) An identifiable intangible asset with a fair value of CU400;

(c) Cash and cash equivalents with a fair value of CU100;

(d) Financial liabilities with a fair value of CU700; and

(e) Deferred tax liabilities of CU160 arising from temporary differences associated with the building and the intangible asset. (See the national or international standards dealing with income taxes.)

IE322. Purchaser pays CU200 for the additional 50% interest in Entity A. Purchaser determines that at the acquisition date the fair value of Entity A is CU400, that the fair value of the non-controlling interest in Entity A is CU120 (30% x CU400) and that the fair value of the previously held interest is CU80 (20% x CU400).

Application of Requirements

IE323. To perform the optional concentration test set out in paragraph AG4B, Purchaser needs to determine the fair value of the gross assets acquired. Applying paragraph AG4B, Purchaser determines that the fair value of the gross assets acquired is CU1,000, calculated as follows:

(a) The fair value of the building (CU500); plus

(b) The fair value of the identifiable intangible asset (CU400); plus

(c) The excess (CU100) of:

(i) The sum (CU400) of the consideration transferred (CU200), plus the fair value of the non-controlling interest (CU120), plus the fair value of the previously held interest (CU80); over

(ii) The fair value of the net identifiable assets acquired (CU300 = CU500 + CU400 + CU100 – CU700).

IE324. The excess referred to in paragraph IE323(c) is determined in a manner similar to the initial measurement of goodwill in accordance with paragraph 85 of IPSAS 40. Including this amount in determining the fair value of the gross assets acquired means that the concentration test is based on an amount that is affected by the value of any substantive processes acquired.

IE325. The fair value of gross assets acquired is determined after making the following exclusions specified in paragraph AG4B(a) of IPSAS 40 for items that are independent of whether any substantive process was acquired:

(a) The fair value of the gross assets acquired does not include the fair value of the cash and cash equivalents acquired (CU100) and does not include deferred tax assets (nil in this example, see the national or international standards dealing with income taxes); and

(b) For the calculation specified in paragraph IE323(c)(ii), the deferred tax liability is not deducted in determining the fair value of the net assets acquired (CU300) and does not need to be determined. As a result, the excess (CU100) calculated by applying paragraph IE323(c) does not include goodwill resulting from the effects of deferred tax liabilities. (See the national or international standards dealing with income taxes.)

IE326. The fair value of the gross assets acquired (CU1,000) may also be determined as follows:

(a) The total (CU1,100) obtained by adding:

(i) The amount paid (CU200) (plus the fair value of the non-controlling interest (CU120) plus the fair value of the previously held interest (CU80)); to

(ii) The fair value of the liabilities assumed (other than deferred tax liabilities, see the national or international standards dealing with income taxes.) (CU700); less

(b) The cash and cash equivalents acquired (CU100); less

(c) Deferred tax assets acquired (nil in this example). In practice, it would be necessary to determine the amount of deferred tax assets to be excluded only if including the deferred tax assets could lead to the concentration test not being met. (See the national or international standards dealing with income taxes.)

Amendment: Part 2 – Recognition of Acquired Liabilities and Contingent Liabilities within the Scope of IPSAS 19

Paragraphs 68, 75, 76 and 77 are amended and paragraphs 75A, 75B, 75C, 77A, 126K, and BC96 are added. A heading is added above paragraph 75A and the headings below paragraph 75 and above paragraph 76 are amended. New text is underlined and deleted text is struck through.

Recognizing and Measuring the Identifiable Assets Acquired, the Liabilities Assumed and any Non-Controlling Interest in the Acquired Operation

…

Recognition Conditions

…

68. Paragraphs AG75–AG84 provide guidance on recognizing intangible assets. Paragraphs ~~76~~75A–82B specify the types of identifiable assets and liabilities that include items for which this Standard provides limited exceptions to the recognition principle and conditions.

…

Exceptions to the Recognition or Measurement Principles

75. This Standard provides limited exceptions to its recognition and measurement principles. Paragraphs ~~76~~75A–84 specify both the particular items for which exceptions are provided and the nature of those exceptions. The acquirer shall account for those items by applying the requirements in paragraphs ~~76~~75A–84, which will result in some items being:

    (a) Recognized either by applying recognition conditions in addition to those in paragraphs 65–66 or by applying the requirements of other IPSAS, with results that differ from applying the recognition principle and conditions.

    (b) Measured at an amount other than their acquisition-date fair values.

Exception<u>s</u> to the Recognition Principle

…

<u>Liabilities and Contingent Liabilities Within the Scope of IPSAS 19</u>

<u>75A. Paragraph 75B applies to liabilities and contingent liabilities that would be within the scope of IPSAS 19, *Provisions, Contingent Liabilities and Contingent Assets*, if they were incurred separately rather than assumed in an acquisition.</u>

<u>75B. The *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* defines a liability as ‘a present obligation of the entity to transfer resources as a result of past events’. For a provision or contingent liability that would be within the scope of IPSAS 19, the acquirer shall apply paragraphs 23–30 of IPSAS 19 to determine whether at the acquisition date a present obligation exists as a result of past events.</u>

<u>75C. A present obligation identified in accordance with paragraph 75B might meet the definition of a contingent liability set out in paragraph 76(b). If so, paragraph 77 applies to that contingent liability.</u>

Contingent Liabilities and Contingent Assets

76. IPSAS 19~~, *Provisions, Contingent Liabilities and Contingent Assets*~~, defines a contingent liability as:

(a) A possible obligation that arises from past events, and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or

(b) A present obligation that arises from past events, but is not recognized because:

(i) It is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; or

(ii) The amount of the obligation cannot be measured with sufficient reliability.

77. ~~The requirements in IPSAS 19 do not apply in determining which contingent liabilities to recognize as of the acquisition date. Instead, the~~ The acquirer shall recognize as of the acquisition date a contingent liability assumed in an acquisition where consideration is transferred if it is a present obligation that arises from past events and its fair value can be measured reliably. Therefore, contrary to paragraphs 22(b), 31, 35, 37 and 38 of IPSAS 19, the acquirer recognizes a contingent liability assumed in an acquisition where consideration is transferred at the acquisition date even if it is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation. Paragraph 115 of this Standard provides guidance on the subsequent accounting for contingent liabilities.

77A. IPSAS 19 defines a contingent asset as 'a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity'. The acquirer shall not recognize a contingent asset at the acquisition date.

…

Effective Date

…

126K. Paragraphs 68, 75, 76 and 77 were amended and paragraphs 75A, 75B, 75C and 77A were added by *Definition of an Operation and Recognition of Acquired Liabilities and Contingent Liabilities* (Amendments to IPSAS 40), issued in October 2026. An entity shall apply those amendments to public sector combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2028. Earlier application is permitted.

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, IPSAS 40.

…

Revisions of IPSAS 40 as a result of *Definition of an Operation and Recognition of Acquired Liabilities and Contingent Liabilities* (Amendments to IPSAS 40)

BC96. The IPSASB reviewed the revisions to IFRS 3 included in the narrow scope amendments titled *References to the Conceptual Framework* (Amendments to IFRS 3) issued by the IASB in May 2020, the IASB's rationale for making these amendments as set out in its Basis for Conclusions and generally concurred that there were no public sector specific reasons for not adopting the amendments.

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