Lease accounting for acquisitions from a business combination

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What causes the need for a fair value exercise?

A business combination, or more commonly known as a takeover, acquisition or merger, is a transaction in which an acquirer (an investor entity) obtains control of one or more businesses. This involves the recognition of identifiable assets and liabilities, which are measured at fair value. This includes any leased assets and liabilities. Whether one business is acquiring another as a subsidiary through ownership rights or purchasing the operations and assets off another, Nomos One can assist when leases are involved.

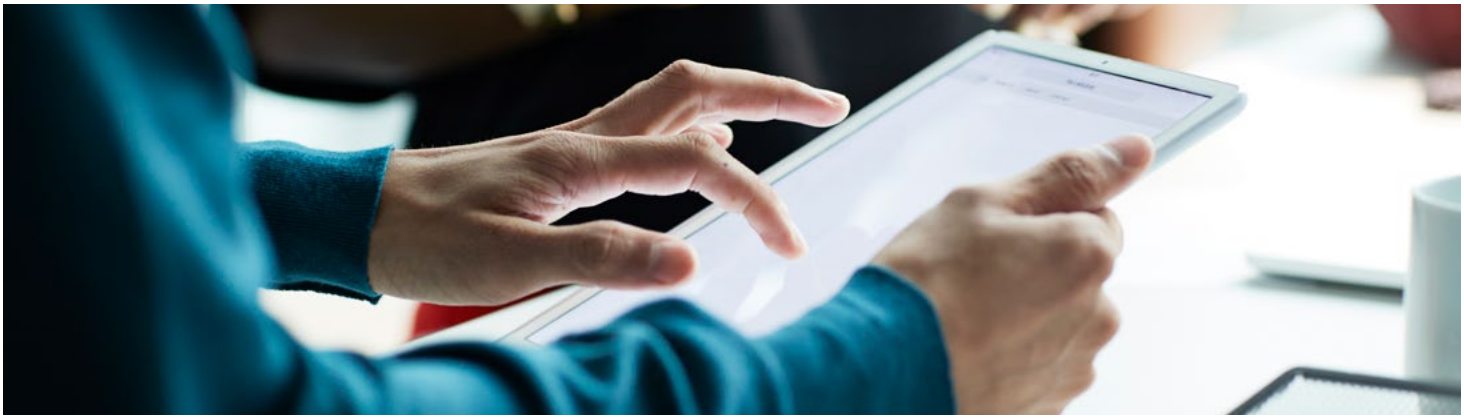
If an asset or liability has a quoted price in an active market (for example, listed shares), this price is used as the fair value. However, few assets and even fewer liabilities have such quoted prices. Fair value then needs to be estimated using a valuation technique, which for leases largely relates to the interest rates and expected lease term of each agreement.

Accounting for leases under IFRS 16 can be complex at the best of times, but additional considerations and management are required when a business combination transaction takes place.

Can Nomos One help?

Our lease accounting software has many functionalities that can be utilised for business combination transactions.

IFRS 16 (Leases) and IFRS 3 (Business Combinations) state that the lease liability on acquisition date will equal the right of use asset amount, treating the lease as if it commenced on this day (IFRS 3; para. 28B). Typically, a reassessment of the interest rate applied to the lease also needs to be completed, as different considerations and factors may impact the rates applicable to the acquired leases.



How Nomos One does it

The first and most simple is the field and settings available for leases acquired through a business combination. These fields have a business combination date and an interest rate that is applied from that date and will calculate IFRS transactions and balances from that date onwards. This works well when leases are onboarded to Nomos One for the first time due to a business combination or for IFRS reporting on acquired leases as it is only required from the date of acquisition.

The alternative to using the business combination field is through the IFRS settings change section of any timeline events. The IFRS settings change section can be used to reflect any non-contractual or judgement changes that may have occurred. This section populates on the completion of any event on the timeline of an agreement and includes fields for a change in the interest rate of an agreement and for any impairment (or reversal of impairment) to the right of use asset. These fields can be used to align the lease liability and right of use on the acquisition date, as noted in IFRS 3.

Nomos One can assist you through the process of updating your existing lease portfolio through a business combination or onboard leases that have been acquired. Our onboarding team specialises in creating and updating lease agreements and can make a fair value assessment straightforward for a business combination.

Follow this checklist to cover the basics of preparing for a fair value exercise from a lease accounting perspective

Preparation	
Review your lease portfolio and lease accounting	
Make sure your events and agreements are up to date	
Determine the list of leases to be included in the fair value exercise	
Fair value exercise	
Confirm the date of the business combination	
Determine any changes in interest rates to be applied to each agreement	
Assess any changes in the expected lease terms for each agreement	
Identify any other estimation / judgement changes	
Define from when ifrs reporting will start, either:	
• From commencement / transition / adoption date, or	
• From business combination / acquisition date	

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