JÖNKÖPING INTERNATIONAL BUSINESS SCHOOL
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IFRS 3, Enlightening the world of Acquisitions

A study of IFRS 3, IAS 36 & IAS 38's impact on companies financial statements and their acquisition process.

Master thesis within Business Administration

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INTERNATIONELLA HANDELSHÖGSKOLAN
HÖGSKOLAN I JÖNKÖPING

IFRS 3, sätter företagsförvärv i nytt ljus

En studie av IFRS 3, IAS 36 & IAS 38's påverkan på företags finansiella rapportering och deras förvärvsprocess.

Magisteruppsats inom Företagsekonomi

Författare: Carlström, Anders
Persson, Tommy

Handledare: Österlund, Urban

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Master Thesis in Finance and Accounting

Title: IFRS 3, enlightening the world of acquisitions – A study of IFRS 3, IAS 36 & IAS 38's impact on companies financial statements and their acquisition process

Authors:	**Carlström Anders, Persson Tommy**
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Date:	**2006-05-30**

Subject terms: Accounting, Finance, IFRS, IAS, Goodwill, Acquisitions, Due Diligence

Abstract

Purpose: The purpose with this thesis is to describe and analyze how the new internationally harmonized accounting standards IFRS 3, IAS 36 & IAS 38 affect the financial statements of companies listed on the Stockholm Stock Exchange and if the new rules have an impact on these firms acquisition practice.

Method: The sample frame of this thesis constitutes of the A-list and the O-list's *Attract 40* of the Stockholm Stock Exchange. From these lists a random sample of 30 companies has been used in order to conduct the research. To fulfill the purpose the authors have used the methodological triangulation approach, i.e. the use of more than one research approach. First, a quantitative method has been used in order to understand how the new accounting standards have effected the companies' financial statements. This research has been conducted by analyzing the companies' annual reports from 2004 and 2005. To be able to examine how IFRS 3, IAS 36 & IAS 38 affect the firms' acquisition practices, the authors used a qualitative, survey-based, method.

Conclusion: The quantitative research found that the new accounting standards have had a significant effect on the companies' financial statements. The operating profits for the 30 companies examined rose with 9.54 per cent or 12.9 billion SEK due to the accounting change. This increase was also evident in the companies' balance sheet where the assets and owners' equity rose with over 7 billion SEK.

In the qualitative research the authors found that companies handle the accounting change in many different ways. The authors have found that the companies that have been most frequently engaged in acquisitions are also the ones that have been putting more effort in the adjustment of their acquisition process and more time to the transformation to IFRS 3, IAS 36 & IAS 38.

A factor that most companies have in common is that they have needed to adjust their standardized acquisition model for the non-amortization of goodwill, dismissals for restructuring costs and the fact that assets need to be valued to its fair value. Furthermore, the fact that the companies now, according to IFRS 3, must identify and separate the intangible assets from the goodwill entry has made the due diligence process more rigorous. The acquisition process will therefore be more time-consuming and require more resources than before.

Magisteruppsats inom Finansiering och Redovisning

Titel: IFRS 3, sätter företagsförvärv i nytt ljus – En studie av IFRS 3, IAS 36 & IAS 38's påverkan på företags finansiella rapportering samt deras förvärvsprocess

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Datum: **2006-05-30**

Ämnesord: Redovisning, Finansiering, IFRS, IAS, Goodwill, Företagsförvärv, Due Diligence

Sammanfattning

Syfte: Syftet med den här uppsatsen är att illustrera och analysera hur de nya, internationellt harmoniserade, redovisningsreglerna IFRS 3, IAS 36 & IAS 38 har påverkat de finansiella rapporterna hos företag noterade på Stockholmsbörsen och om de nya reglerna har haft en påverkan på dessa företags förvärvsprocess.

Metod: Populationen från vilken författarna har tagit sitt urval i denna uppsats består av Stockholmsbörsens A-lista, samt O-listans *Attract 40*. Från dessa listor har ett slumpmässigt urval av 30 företag valts. För att uppfylla uppsatsens syfte har författarna använt den metodologiska triangulering, det vill säga använt flera forskningsmetoder. Först har en kvantitativ undersökning gjorts för att förstå hur de nya redovisningsreglerna påverkat företagens finansiella rapporter. Detta har genomförts genom att undersöka årsredovisningar för åren 2004 och 2005. För att förstå hur dessa regler påverkat företagens förvärvsprocess har även en kvalitativ, enkätundersökning utförts.

Slutsats: Den kvantitativa undersökningen visade att de nya redovisningsreglerna har haft en stor påverkan på företagens finansiella rapporter. Rörelseresultatet för de 30 företagen i undersökning ökade med 9.54 procent eller 12.9 miljarder SEK på grund av redovisningsreglerna. Denna tendens visade sig också i företagens balansräkning där tillgångarna och det egna kapitalet ökade med över 7 miljarder SEK.

I den kvalitativa undersökningen visade det sig att företagens sätt att hantera de nya reglerna varierade stort. De företag som oftast var inblandad i förvärv är också de som har visat upp störst ansträngning för att anpassa sin förvärvsprocess efter de nya redovisningsreglerna IFRS 3, IAS 36 & IAS 38.

En faktor som en majoritet av företagen har gemensamt är att de har varit tvungna att anpassat sina standardiserade förvärvsmodeller på grund av de nya reglerna. Vidare så har det faktum att företagen enligt IFRS 3 måste identifiera och särskilja immateriella tillgångar från goodwill, bidragit till att göra företagens due diligence process mer omfattande och tidskrävande än innan de nya reglerna.

Abbreviations

BFN	The Swedish Accounting Standards Board (Bokföringsnämnden)
FAR	The Institute of Public Accountants (Föreningen Auktoriserade Revi sorer)
IAS	International Accounting Standards
IASB	International Accounting Standards Board
IASCF	International Accounting Standards Committee Foundation
IFRS	International Financial Reporting Standards
RR	The Association for the Development of Generally Accepted Accounting Principals (Redovisningsrådets Rekommendationer)
SOU	The Swedish governments Public Investigations (Statens Offentliga Utredningar)
US GAAP	The United States Generally Accepted Accounting Standards
ÅRL	The Annual Accounts Act (Årsredovisningslagen)

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1 Introduction

"Acquiring companies – knowing your International Accounting Standards from your elbow"

Stevenson & McPhee, 2005, pg 82

1.1 Background

According to an article in *Dagens Nyheter*, a leading newspaper in Sweden, almost ten percent of the profits of the quoted companies in 2005 are a result of the new goodwill[1] rules. This implies that approximately 70 billion SEK of the profits are a result of the new accounting rule on goodwill. (Rognerud, 2006)

Svenska Dagbladet, another leading newspaper in Sweden, comes to the same conclusion and states that investors should take a more sceptic approach when studying quarterly – and annual reports after the implementation of the new accounting standards. This due to the fact that the companies earnings are 8 – 9 per cent higher due to the accounting change. (Suneson, 2005)

Investors' confidence in the quality and integrity of company's financial reporting is of crucial importance in order to maintain efficiency on the capital market. This since investors rely heavily on the companies' stated earnings, assets and liabilities when valuating companies which in turn affect the companies stock prices and the perceived image of the firm. (Lev, 2003).

The world has changed rapidly during the last decades and so have the accounting principles. The trend in the world of accounting is now towards more harmonization and convergence between different countries. For a company conducting its operations in a purely domestic environment and including domestic owners, it poses no major problems that the financial statements are not presented in the same way as in foreign companies. When it comes to international business transactions, however, it is inconvenient, inefficient and costly that individual country rules vary significantly. The globalisation of capital markets and growth of companies have not only led to a demand for accounting harmonization, but also to an increase in the number of acquisitions. (Schwenke, 2002)

The demand for a common accounting standard led to the creation of a new international accounting standard which was implemented on January 1st, 2005. The new standards, International Financial Reporting Standards (IFRS) & International Accounting Standards (IAS), imply that quoted[2] companies within the European Union must prepare their consolidated accounts in conformity with the new standards. (SOU 2003:71)

The organization behind this new standard is the International Accounting Standards Board (IASB) which is the setting body organization of the International Accounting Standards Committee Foundation (IASC Foundation). The objectives of the IASC Foundation

[1] An intangible asset which provides a competitive advantage, such as a strong brand, reputation, or high employee morale. In an acquisition, goodwill appears on the balance sheet of the acquirer in the amount by which the purchase price exceeds the net tangible asset of the acquired company (Investorwords, 2006).

[2] Quoted companies are those whos shares are listed on a regulated market in a member state in accordance with article 1.13 of the investment directive 93/22/EEG (SOU 2003:71)

are to develop a single set of high quality and understandable global accounting standards which require high quality, clear and equivalent information of financial reporting. (KPMG, 2004) The target for these objectives is to contribute to an appropriate and efficient capital market, to improve the free movement of capital and to create conditions for companies in the European community to compete equally. (SOU 2003:71)

According to a report made by the auditing and consulting firm KPMG (2003), the new accounting standards will especially have a key impact on companies engaging in acquisitions. This since the procedure for consolidation and acquisitions has changed with the new international accounting standards IFRS and IAS (KPMG, 2003).

The main features of the new rules for acquisitions are stated in IFRS 3 *Business Combinations* which prohibits the amortization of goodwill. Closely connected to IFRS 3 are the standards IAS 36 *Impairment of Assets* and IAS 38 *Intangible Assets*. The combination of these rules states that goodwill must now instead be tested annually for impairment and it also requires intangible assets acquired as part of an acquisition to be identified, valued and amortizised over their useful lives. (Spillane, 2005)

1.2 Problem Discussion

In a competitive business it is of crucial importance for companies to create sustained advantages. One way to create advantage is through acquisitions. Peter Malmqvist, chief analyst of the Swedish stock-broker Nordnet, claims in *Svenska Dagbladet* that the new accounting standards regarding goodwill will primarily have a significant impact on large companies who are frequently engaged in acquisitions (Bergin, 2006).

According to an article by Ernst&Young (2006) the number of acquisitions in Sweden increased with 15% to 103 in 2005. In particular, large Swedish corporations are increasing their efforts to invest both domestically and in foreign markets. This is partly due to the rise in the overall economy and the fact that the stock-market has been flourishing in 2004 and 2005 (OMX, 2006).

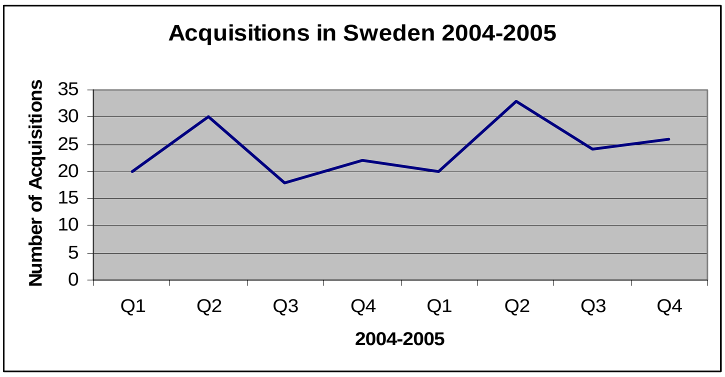


Figure 1- Acquisitions in Sweden 2004-2005 (Ernst&Young, 2006)

According to a recent survey by PricewaterhouseCoopers (2006), investors say that the new international accounting standards IFRS 3 regarding acquisitions is having a real impact on the way they perceive companies and consequently on their investment decisions. Furthermore, Ian Wright, Global corporate reporting leader at PricewaterhouseCoopers (2004), states that the new accounting standard will lead to increased transparency that will give the market greater insight into what has actually been acquired. Markets will be able to judge the success or failure of acquisitions more quickly and more accurately. He further argues that the changes to accounting standards may transform the way companies handle, plan and execute acquisitions. Finally, Wright claims that the core of the new rules, which includes impairment testing, transparent cost allocation and extra disclosures, will require an extra investment in time and resources for each investment. (PricewaterhouseCoopers, 2004)

IFRS 3 was as already mentioned introduced on January 1st 2005 and this implies that most quoted Swedish companies[3] in 2006 present their first consolidated annual reports in conformity with IAS/IFRS. However, all quoted companies have been obliged to present a comparison between their financial figures under the old regulation and IAS/IFRS since January 1st 2004. This implies that the affect of IAS/IFRS appeared first in 2004's annual reports and that, starting in 2005, companies will only report according to IAS/IFRS.

Even if there are some reports that have tried to predict the outcome of the new standards in advance, there are few reports that have yet identified or studied the real effects that these new accounting standards have had on the financial statements and on the acquisition process for Swedish firms. Hence, this can easily be explained by the fact that Swedish companies have only been presenting their reports in conformity with the new standards for a year. Because of this, the authors of this thesis find it especially interesting to study the real effects of these changes by addressing the following question:

- *How have the new accounting standards IFRS 3, IAS 36 & IAS 38 regarding acquisitions affected the income statements and the balance sheets of the quoted companies?*

The authors will develop this research further by dividing the quoted companies into industries in order to see if the new rules affect the industries differently.

With the above stated research question and the recent studies from e.g. PricewaterhouseCoopers (2006) and KPMG (2003) in mind the authors also wishes to address:

- *What effects do the new standards have on the Swedish firms' acquisition process and how do the companies handle these changes?*

1.3 Purpose

The purpose with this thesis is to describe and analyze how the new internationally harmonized accounting standards, IFRS 3, IAS 36 & IAS 38 affect the financial statements of the companies' listed on the Stockholm Stock Exchange and if the new rules have an impact on these firms' acquisition practice.

1.4 Perspective

This thesis is written from an investor's perspective, investors being either individuals or institutions. This since the purpose of financial reporting is to give investors accurate information of the company's financial status. This thesis can also be seen from a corporate perspective where acquisition managers can gain insights on how the new accounting standard affects the acquisitions process. Furthermore, as already mentioned there are few

[3] The membership-states can decide that some companies do not need to apply the current accounting standards in their consolidated reports until January 2007. The companies that can use this exemption are firms that only have instruments of debt quoted and organizations that are quoted both in the EU and on a market outside the union (SOU 2003:71).

studies that have yet identified the true effects of IFRS 3 on the acquisition process. Thus, this thesis can also be used from a theoretical perspective by offering a foundation for future studies.

1.5 Delimitations

In this thesis, only the accounting standards IFRS 3 *Business Combinations,* IAS 36 *Impairment of Assets* and IAS 38 *Intangible Assets* will be looked upon and analyzed, this since they are the standards closely connected to acquisitions and the changes therefore can be isolated and identified.

Furthermore, the tax issue connected to the new accounting standards will not be regarded when doing the comparison and analysis. This since it is hard to isolate the tax effect of IFRS 3, IAS 36 and IAS 38 from the other new accounting standards. This goes beyond the scope of this thesis since tax issues are advanced and companies handle them in different ways and thus would require a thesis of its own.

1.6 Definitions

When the authors refers to the term acquisition in this thesis it is defined as a situation where a parent company (the acquirer) acquires so many shares in the subsidiary (the acquired company) that the former gains a dominant influence (which usually is more than 50 percent of the shares).

1.7 Literature Study

The authors have used several sources in order to retrieve the information. These sources include research journals, books, publications from the large accounting firms and legislative texts. The search for articles regarding the new accounting standards and its effect on companies' acquisition process were done mainly through the databases JSTOR and ABI-Inform. Examples of search words used to limit the amount of information when searching for applicable articles were "IFRS 3", "IAS", "Business Combinations", "Acquisitions", "Acquisition strategy", "Valuation of acquisitions", "Premiums", "Goodwill" and a combination of these.

The type of literature most used in this thesis is publications within accounting from the International Accounting Standards Board. This because IASB is the founder of the international accounting standards and thereby possesses the primary knowledge of their implications. Furthermore, publications from the Swedish Institute of Public Accountants have been used in order to understand the special treatment of accounting in Sweden.

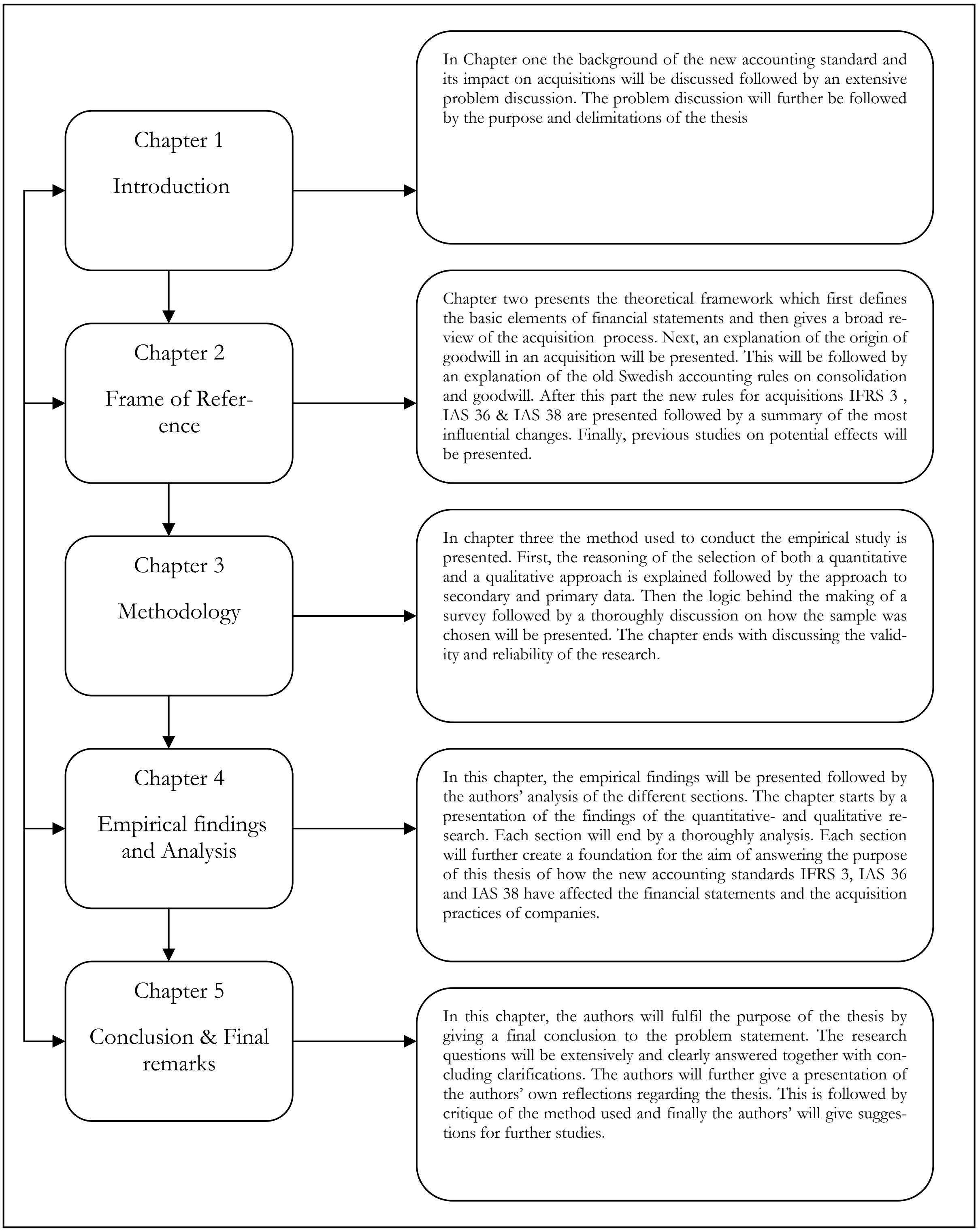
Moreover, the authors have used several publications from large auditing and consultant firms such as Deloitte, KPMG, PricewaterhouseCoopers and Ernst&Young. This due to the fact that these firms have great knowledge of the new accounting standards and work closely with companies with their implementation of IFRS 3. Thereby giving them an inside perspective on the implications of the new standards.

Books within acquisition theory have been used in order to understand the accounting standards affect on the acquisition process. This has mainly included books within the field of corporate finance.

The annual reports used to analyze the differences in financial statements where gathered using primarily the companies websites. This information is the same as in the printed version and the reason for using it is that it is faster to retrieve.

1.8 Disposition

The disposition highlights and visualizes the succession of the chapters and the structure of the thesis. The purpose is to give the reader a fundamental overview of the structure of the thesis.



2 Theoretical Framework

This chapter constitutes the theoretical framework on the concept of financial statements, accounting standards and acquisitions. Starting with an overall view of financial statements and goodwill and continuing with a more in-depth look at the accounting standards of today, how they have changed and what effect they have on the accounting for acquisitions. The chapter ends with previous studies regarding the new accounting standards impact on the company's acquisition process.

An acquisition occurs when a company purchases the assets or shares of another business and with the acquired firm's shareholders ceasing to be owners of that firm (Sudarsanam, 1995).

After an acquisition the question of consolidation becomes applicable. Consolidation is based on control, which in this field means the power to govern the financial and operating policies of a unit in order to gain benefits from its activities. (KPMG, 2004) Consolidation is applicable for business combinations, that is the bringing together of separate entities into one economic unit as a result of one entity obtaining control over the net assets and operations of another entity (Van Gruening, 2005).

With the new international accounting standards IFRS and IAS, the procedure for consolidation and acquisitions has changed (KPMG, 2003).

2.1 Financial Statements

In order to understand how the new accounting standards affect companies, one must first have an understanding of the function of financial statements.

Financial statements consist of primarily three parts, the balance sheet, the income statement and the statement of cash flow (White, Sondhi & Fried, 1998). The financial statements have an important meaning for many stakeholders but it differs in how it is used by them. Investors are mainly interested in the valuation and profitability of a firm, while creditors are concerned with the firm's ability to repay debt. Management is interested in assessing the overall efficiency of the firm, i.e. efficiency on items ranging from operations, to the use of assets and debt. (Tempte, 2005) In the following section the authors will present the three parts that make up the financial statement.

2.1.1 The balance sheet

The balance sheet is a statement of financial position and reports major classes and amounts of assets, liabilities and stockholders' equity (White et.al. 1998). Assets represent everything of value for the firm. Assets can be tangible items such as buildings, raw materials, finished products for sale, and real estate. Other items of value that are owned by the firm but not tangible are also considered assets. These include money that is owed by others to the firm, known as accounts receivable and other intangible assets such as patents, trademarks and client lists. (Tempte, 2005) Assets are financed directly or indirectly by the firm's creditors or stockholders. This is the fundamental accounting principal that:

Asset (A) = Liabilities (L) + Stockholders' Equity (E)

(White et.al. 1998)

Liabilities represent debts or obligations owed by the firm to another entity. For example, one way that firms can purchase assets for business is by obtaining credit from others. Other examples are salaries owed to employees or taxes owed the government. Stockholders' equity on the other hand is everything that is owned by the firm subtracted by everything that is owed by the firm. Most common types of accounts under stockholders' equity are common stock, preferred stock, and retained earnings. (Tempte, 2005)

2.1.2 The income statement

The income statement is a statement of earnings and reports the result of the firm's operating activities. This is done by taking the revenues from the firm's sales or services and subtracting by the expenses for that same period. The income statement gets a lot of attention from financial analysts because it answers the question, "Did the company make a profit?" (Tempte, 2005). This profit/loss is presented in the bottom line of the income statement and represents the firm's result for the given period. The income statement explains some of the differences in the balance sheet between two consecutive balance sheets date. (White et. al. 1998)

2.1.3 The cash flow statement

The cash flow statement reports cash receipts and payments in the period of their occurrence. It summarizes the changes in the firm's cash account and shows the cash flow changes from operations, investments, and financing. Operating cash flows are those that result from the operations of the business. Positive cash flow from operations is essential for every organization's longevity. If an organization is unable to generate positive cash flows from operations, it will eventually be forced to shut down either voluntarily or involuntarily through bankruptcy. (Tempte, 2005)

2.1.4 The use of financial statements

As mentioned before, the firms' different stakeholders are looking for different things in the financial statement. Investors are mainly concerned with the value of the firm and how profitable it is, this in order to get a good return on their invested capital. Creditors are most concerned with the corporation's ability to repay principal and interest on debt. Corporate bankers, bondholders, and trade creditors focus on the cash flow of the organization over the life of the debt. (Tempte, 2005)

Management use the financial statements to identify the overall profitability, efficiency, and direction of the firm, this in order to increase shareholder value. Additionally, the financial statements are prepared for and used to analyze specific segments, product lines, and divisions of the organization. Management is the primary user of financial statements and employs the information to make strategic and operating decisions, like acquisition strategies. (Tempte, 2005)

2.2 Acquisitions

Merger and acquisition (M&A) activity has increased significantly since the early 1990s (Gupta & Gerchak, 2002). The only drop in this trend came after the IT-bubble burst in the 2000. The trend today is towards large multinational combinations. One of the most recent examples of this trend is the merger between Alcatel (France) and Lucent (USA), two large, multinational, telecom companies. (Grundberg, 2006)

2.2.1 What is an acquisition and why does it take place?

The fundamental objective behind acquisitions, like all other strategic decisions, is that it should increase shareholders' wealth by adding value to the company (Kristensen, 1999; Sudarsanam, 1995). An acquisition can achieve this objective by, for example, creating synergies, adding to the growth of the firm, gaining competitive advantage in existing products or markets or by reducing the firm specific risk. Acquisitions are usually of such financial and strategic magnitude that it needs to be placed in the context of the firm's broader corporate and business strategy framework. (Sudarsanam, 1995)

Placed in the corporate framework a great deal of management time and attention is dedicated to acquisitions with the expectation of large, lasting payoffs (Triantis, 1999). This due to the fact that the right acquisition at the right time can create advantages in many forms such as increased profitability or a larger market share (Morris, 2000).

There is no single reason for companies to acquire other businesses but the most common motive for acquisitions is the expectation of synergy effects (Morris, 2000).

Synergies
Synergy is the idea that the value and performance of two companies combined will be greater than the sum of the separate individual parts (Morris, 2000). It is the additional value that is generated by combining two firms, creating opportunities that would not been available to these firms operating independently. Synergy can be divided into two groups, operating and financial synergies. Operating synergies affect the operations of the combined organizations and include economies of scale, an increased pricing power and a higher growth potential. Financial synergies, on the other hand, are more focused and include tax benefits, diversification, a higher debt capacity and uses for excess cash (Damodaran, 2005). This can be achieved through, for example, consolidation of operations, such as research and development, through new distribution channels or a more effective product development. To summarize the above discussion, the general idea of synergies is that the acquirer achieves an enhanced financial and competitive performance after the acquisition. (Triantis, 2000)

Other common reasons for acquisitions are described in the following section:

Faster Growth
By acquiring other businesses the company can accelerate its growth process and thereby quickly increase market shares, achieve economies of scale by, for example, using the same management team or research facilities or increase company recognition (Morris, 2000). According to Olve (1988) this strategy works best when the acquisition is attractive for both the acquirer and the target firm. If the acquisition is attractive for both parties it is more likely to create lasting synergy affects.

Vertical or Horizontal Integration
If, for example, a manufacturing company wishes a more thoroughly control of its supply it can engage in vertical integration, meaning that its main suppliers are acquired to achieve a more stable and controllable outlet for its products. (Morris, 2000) Horizontal integration on the other hand takes place when a company who wishes to extend its market share or

gain access to a new market acquires a competitor. This way the company can gain market shares more rapidly. (Morris, 2000)

Acquisition of intangibles and personnel
By acquiring another business, the acquiring firm incorporates the knowledge and personnel into its organization. This may include such things as technology, patents, a marketing network, contracts or key people that it would be very hard for the company to duplicate on their own. (Morris, 2000)

Portfolio investment
A company that wants to invest excessive cash at a higher rate than what is available through regular cash accounts or existing investments can acquire another firm without hopes of synergy effects but merely the objective that it will generate high returns. (Morris, 2000)

Diversification
Another reason for an acquisition may be to gain entry to an entirely new line of business. This is done to limit the company risk by being active on several markets within different industries. (Morris, 2000) By using this strategy the acquiring firm can also get around the other often expensive entry barriers such as economies of scale, product differentiation, absolute cost and capital requirements. (Hopkins, 1987).

2.2.2 The acquisition and due diligence process

When the overall strategy of the acquirer is determined, the firm has to focus on how the actual acquisition will be conducted and how much they are willing to pay for the target firm. This is done by first conducting a due diligence. Due diligence is a process made by the investor or acquirer in order to obtain or verify information about an acquisition candidate. This process is carried out by reviewing not merely the information presented by the target firm, but also by conducting an independent investigation in order to confirm the information. The due diligence should include such procedures as a review of public records to determine title to assets, inspection of internal documents, review of contracts of leases and loan documents, physical inspection of tangible assets and verification of financial statements. It is also important to investigate less obvious matters such as potential environmental problems, stability of supplier relations and customer loyalty. The time and resources allocated for due diligence vary with the size of the acquisition. That is, the larger the acquisition the more thoroughly is the due diligence process. (Morris, 2000)

When the decision to acquire has been taken, the next steps in the acquisition process are to structure the acquisition and to establish a price (Morris, 2000). The authors will in the following sections describe the process of structuring and pricing the acquisition.

2.2.3 Structuring the acquisition

The structuring of acquisitions focuses on the method of acquisition, i.e. whether to purchase only the assets of the target firm or to buy the stocks. The term asset purchase means that the buyer purchases the assets of the target firm, not the corporation or other legal entity owned by the seller (Morris, 2000). There are two principal advantages to an asset acquisition. First, in terms of tax treatment, most acquired companies have a basis in their assets that is lower than the fair market value of the assets. Secondly, by purchasing the assets only, the buyer might avoid potential contingent liabilities of the acquired business. (Sudarsanam, 1995)

When it comes to stock purchase it usually entails the disadvantage of carrying forward a lower basis in assets, the possible inadvertent exposure to corporate liabilities, including undisclosed contingencies and the need to deal with substantially all the assets and liabilities instead of being able to pick and choose those which the parties wish to transfer. (Sudarsanam, 1995) Advantages to stock purchase is mainly that it is mechanically easier to buy the entire firm instead of splitting the target firm into many different items that each has to be dealt with separately. (Morris, 2000)

2.2.4 Valuation of acquisitions

When the method of purchase is decided the next step is to establish a price for the target firm. This is done through a valuation of the target firm, using the figures retrieved through the due diligence process as a foundation. The most common methods for valuation of firms are those based on cash flow projections, earnings or assets. (Sudarsanam, 1995)

Discounted cash flow valuation

The discounted cash flow model is the most frequently used method and is conducted in a number of steps. This method is trying to estimate the future cash flows of the target company within a preset horizon in order to determine what return on the investment the buyer will receive from the acquisition candidate (Morris, 2000).

The actual procedure of this valuation method consists of several parts. First, the future cash flows must be recognized through estimation. This is done through forecasts of the value drivers of the target, i.e. the key revenues, costs or investment variables that determines the cash flow. This includes finding a terminal value for the target at the end of the time horizon. When the cash flow and the terminal value is projected, an appropriate discount rate must be determined. The discount rate most frequently used is the weighted average cost of capital[4] (WACC) which takes into account factors such as risk and capital structure of the acquirer. (Sudarsanam, 1995)

When the appropriate discount rate is set, the value of the target firm can be determined by discounting the cash flows and the terminal value by this rate. Through these steps the acquirer receives a present value of the target firm, which is how much all future cash flows are worth today, i.e. the value of the target today. (Sudarsanam, 1995) The actual formula for this looks as follows:

$$V_a = \Sigma\, CF_t/(1+WACC)^t + TV_t/(1+WACC)^t$$

V_a = Value of the target firm
CF_t = Cash Flow of target in period t
TV_t = Terminal Value of target at t

(Sudarsanam, 1995)

Earnings valuation

The earnings valuation method is based on the price-to-earnings ratio (P/E), and expresses the relationship between a firm's earnings and its market capitalization. The P/E is a function of the level of future equity earnings of the firm, the investors expected return for eq-

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4 The actual formula for the weighted average cost of capital is: $r_{wacc}= (S/(S+B))*r_S+((B/(S+B))r_B(1-T_c)$, where S=Equity, B=Debt, r_S=Cost of Equity, r_B=Cost of Debt, T_c=Corporate Tax rate

uity investments, the expected return on the investments made by the firm and the length of time the firm can earn returns on its investments in excess of the investor-required return. (Sudarsanam, 1995) During takeover bids the P/E ratio is often cited by both acquirer and targets to indicate whether the price being offered is generous or not (Morris, 2000)

Asset valuation
The assets based valuation of a firm is based on the relationship between the assets of the firm and its market value. The market value is often referred to as the replacement cost of the asset, i.e. the cost of buying an asset of identical characteristics. (Sudarsanam, 1995)

2.2.5 Premiums

The difference between the actual costs for acquiring a target firm versus the estimate made of its value before the acquisition is called premium. That is, the percentage difference between the trading price of the target's stock before the announcement of the acquisition and the price per share paid by the acquirer (Haunschild, 1994). Premiums are major statements by acquiring managers of how much additional value they can extract from the target firm. The premium is an important part of an acquisition since it according to Sirower (1994, cited in Hayward & Hambrick, 1997) affects the acquirer's shareholders' returns for up to four years after the acquisition and the higher the premium paid is, the lower is the ultimate returns for the acquirer. The premium paid by the acquirer should reflect the information retrieved through the due diligence process and should be based on information such as the value of the targets fixed assets, intangible assets, current and future earnings (Morris, 2000).

Premiums underscore acquiring managers convictions that the target's preexisting stock price inadequately reflects the value of the firm's resources and its prospects, and that with better management more value can be created (Hayward & Hambrick, 1997). Generally, the greater the expected synergies or other structural benefits from the acquisition are, the greater is the premium paid (Haunschild, 1994; Morris 2000). According to Haunschild (1994) firms pay a 50-percent premium on average, but premiums exceeding 100-percent are not uncommon.

The premium paid in an acquisition is accounted for as goodwill in the acquirer's balance sheet. The accounting standards and regulations will be discussed further in the next section.

2.3 Accounting for Acquisitions

2.3.1 Goodwill

Goodwill is an intangible asset that appears in a company's balance sheet (White et. al. 1998). One of the major changes in the new accounting standards affects the treatment of goodwill arising from acquisitions. Thus the authors will first give the reader the basic details of goodwill, which will assist the reader throughout the theoretical framework.

As the following quote by Stephen Gilman reveals, the treatment of goodwill has been a controversial issue within the accounting field for decades.

"No one can afford to be dogmatic about the treatment of goodwill. So many excellent authorities disagree absolutely as to the treatment of goodwill that it would seem as almost any of the methods discussed would be justifiable"

(Stephen Gilman, 1916, quoted in Nilsson, 1998, p 195)

When a company acquires another company something called goodwill can arise. The definition of goodwill is according to Investorwords (2006), "*An intangible asset which provides a competitive advantage, such as a strong brand, reputation, or high employee morale. In an acquisition, goodwill appears on the balance sheet of the acquirer in the amount by which the purchase price exceeds the net tangible asset of the acquired company*".

Goodwill that has been acquired in an acquisition represents the payment for future economic benefits from assets that are not capable of being individually identified and separately recognized. Goodwill is measured as the residual cost of the acquisition after recognizing the acquired entity's identifiable assets, liabilities and contingent liabilities. (Spillane, 2005)

When an acquisition is accounted for, the cost of the acquisition must be set off against the net assets of the subsidiary. Hence, the measurement of the cost of the acquisition is of vital importance in accounting for acquisitions. It also has a direct influence on the measurement of goodwill in the consolidated balance sheet.

In order to give a straightforward illustration of goodwill the following simplified example shows the nature of how it appears in an acquisition at the set-off date:

The cost of the acquisition:	100
Fair value of the net assets of the subsidiary:	60
Consolidation difference (goodwill)	40

In most of the acquisitions goodwill is recognized but in a few cases negative goodwill are acknowledged instead. Negative goodwill is defined as the difference between the cost of the acquisition and the higher value with which the identifiable net assets of the subsidiary are actually capitalized in the consolidated financial statements.

The following simplified example gives an example of how negative goodwill appears in an acquisition at the set-off date:

The cost of the acquisition:	150
Fair value of the net assets of the subsidiary:	180
Negative goodwill:	30

(Schwenke, 2002)

Goodwill resulting from acquisitions is according to Malmqvist (2002) one of the most controversial fields within the accounting area. The much-debated question has been not only about if the post should be reported in the balance sheet but also how the post should be reported.

Nilsson (1998) gives in his doctoral dissertation the following view in a similar way about the accounting for goodwill in Sweden; *"Every conceivable manner of accounting in the same coun-*

try, at the same time". This view stems from the fact that the companies during the 1980's and the 1990's handled the issue of goodwill in very different ways and with different methods. At this time some companies followed German rules, amortizing their goodwill over no more than ten years. Some companies, however, referred to the rules in the United States, extending the amortization to forty years. Yet other firms were more influenced by British accounting, by writing off their goodwill immediately against owners´ equity. (Nilsson, 1998)

2.3.2 Legislation in Sweden before IFRS/IAS

In order to gain insights of the changes made in the accounting principles it is important to look at how companies reported their consolidated accounts before 2005. It is also of crucial impact to describe the legislation affecting the accounting of Swedish companies

As in other European countries, the information function is the most important financial reporting function in Sweden. The main purpose of financial reporting is to give a true and fair view of the transactions and financial information of companies. When it comes to the general accounting principles in Sweden it is regulated not only by legislation but also by norms that are not formally binding by the courts, but instead they might have considerable legal weight. (Schwenke, 2002)

Important in Sweden when it comes to the treatment of accounting is especially two well accepted general accounting norms. The first is the national implementation of *true and fair view*. The principle of true and fair view is used in some special cases, where application of general advices and recommendations from a norm setter, is regarded in conflict with this view. The second principle is the legal norm *good accounting principles* which reflects the actual accounting practice among a qualitative representative group of companies. These principles are often included in accounting recommendations. Both of these norms are used as guidelines regarding the treatment of accounting. (Schwenke, 2002)

The accounting legislation in Sweden consists of mandatory accounting acts, the Annual Accounts Act of 1995 and the Book-keeping Act of 1999 being the most important ones. Both the Annual Accounts Act and the Book-keeping Act are general frameworks for accounting and both acts refer to "generally accepted accounting principles". (BFN, 2006)

Until IFRS/IAS was introduced, Swedish companies reported their consolidated accounts in accordance to RR 1:00. This is a norm that was issued by the Association for the Development of Generally Accepted Accounting Principles (RR). The recommendations of this association were applicable for all quoted Swedish firms that according to a contract with the Stockholm Stock Exchange, not without a reasonable reason can diverge from these commendations. (Artsberg, 2003)

The recommendations in RR 1:00 states that goodwill has an expandable useful life through time and therefore should be amortized systematically through time. According to this recommendation, goodwill has a useful life of maximum twenty years. It is up to the companies to decide useful life though. RR 1:00 also states that goodwill should be reported in the balance sheet by its true value with a reduction of accumulated amortization and eventual impairment. (FAR, 2005)

Swedish companies also reported goodwill through legislation, according to the annual account act ÅRL 4th chapter 2 §, as an intangible asset which have to be amortized systematically over its useful life. An intangible asset is according to RR 15 an identifiable, nonmonetary asset without physical substance that is possessed in order to be used in the production, or to supply goods or services, and for rental or administrational purposes. (FAR, 2005)

In order to account for intangible assets separately in an acquisition, RR 15 demands that these assets are expected to be identified and also that they need to give economical advantages in the future. Since most people argue that intangible assets in an acquisition are not satisfying these demands it is therefore included in the goodwill post. (Jansson, Nilsson & Rynell, 2004)

The amortization of goodwill and other intangible assets should be reported as a cost in the income statement. According to ÅRL 4^{th} chapter 4 §, is the useful life for an intangible asset five years if not a dissimilar time with reasonable degree of certainty can be established. The same paragraph also states that if a longer time than five years is used, a note in the financial statement will have to give information about this. (FAR, 2005)

2.3.3 Today's rules regarding business combinations, according to IFRS 3.

As mentioned in chapter 1, all listed companies are obliged to establish their consolidated reporting in accordance with IFRS/IAS (IASCF, 2002).

According to Schwenke (2002), transactions involving business combinations comprise areas where accounting principles traditionally differ significantly between countries.

In March, 2004, the IASB issued a new standard regarding acquisitions, IFRS 3 *business combinations*. The objective of the issuance was to improve the quality of, and seek international convergence on, the accounting for business combinations regarding goodwill and intangible assets. When introducing this standard Sir David Tweedie, IASB Chairman, said: *"Accounting for business combinations diverged substantially across jurisdictions. IFRS 3 marks a significant step towards high quality standards in business combination accounting, and in ultimately achieving international convergence in this area"*. (IASB, 2004)

IFRS 3 *business combinations* have also been developed in order to require a methodology of accounting for business combinations that provides users with the most accurate and useful information. Another object has been to convert the requirements of IFRS as closely as possible to American standards such as US GAAP. Closely connected to the standard IFRS 3 are IAS 36 impairment of assets and IAS 38 intangible assets. The introduction of IFRS 3 together with IAS 36 and IAS 38 completes the major objectives of IASB and provides a consistent and fair framework to be used for business combinations. These three standards accompany each other. (Deloitte, 2004)

2.3.4 How to identify a business combination according to IFRS 3

The objective of IFRS 3 is to specify the financial reporting by an entity when it undertakes a business combination. The result of nearly all business combinations is that one entity, the acquirer, obtains control of one or more other businesses, the acquired company.

If an entity obtains control of one or more other entities that are not businesses, the bringing together of those entities is not a business combination. (IASCF, 2004)

In order to determine whether a transaction should be accounted for in accordance to IFRS 3 the entity should consider whether the items acquired can be assumed to meet the definition of a business. A business is in this case defined by IFRS as an integrated set of activities and assets conducted and managed for the purpose of providing:

- A return to investors; or
- Decreased costs or other economical benefits directly and proportionately to policyholders and other participants.

(IASCF, 2004)

The following types of transactions are examples that normally meet the definition of a business combination.

- The purchase of all the assets, liabilities, and rights to the activities of the entity.
- The purchase of some of the assets, liabilities, and rights to the activities that together meets the definition of a business (see above).
- The establishment of a new legal entity which will hold the assets, liabilities and the activities of the combined business.

(IASCF, 2004)

A business combination will further result in a parent-subsidiary relationship where the acquirer is the parent and the acquired company is a subsidiary of the acquirer. In such conditions, the acquirer applies IFRS 3 in its consolidated financial statements. It includes its interest in the acquired company in all the separate financial statements it issues as an investment in a subsidiary. (IASCF, 2004)

2.3.5 Method of accounting

There has been a significant debate about the appropriate method of accounting for business combinations. Two methods have been commonly accepted, pooling of interests and the purchase method. Under the pooling of interests method the assets and liabilities of the combined entities are carried forward to the combined accounts at their existing carrying accounts, and the combined accounts are existing as if the entities have always been combined. (Deloitte, 2004)

The purchase method means that an acquirer must be identified; that the cost of the acquisition is measured at its fair value, as the assets, liabilities, and contingent liabilities of the acquired company at the date of the acquisition (KPMG, 2004).

Under IFRS 3, all business combinations must be accounted for by using the purchase method. The pooling of interests method that was allowed in some earlier circumstances are not allowed anymore for transactions which have an agreement date later than March 31st 2004. (KPMG, 2004)

At the date of the acquisition the acquirer should recognize goodwill acquired in a business combination as an asset. (IASCF, 2004)

2.3.6 Main features of IFRS 3

The main characteristics of IFRS 3 are presented below:

Cost of acquisition
IFRS 3 requires that an acquirer quantify the cost of a business combination as the aggregate of the fair values, at the date of the exchange, regarding assets given, liabilities incurred, and equity instruments issued by the acquirer. The cost for the acquisition is given in exchange for control of the acquired company; plus the costs directly attributable to the combination. (IASCF, 2004; KPMG, 2004)

Quantification and identification of assets, liabilities and contingent liabilities
IFRS 3 requires an acquirer to identify separately, at the acquisition date, the acquired company's identifiable assets, liabilities and contingent liabilities regardless of whether they had been previously recognised in the acquired company's financial statements. They will have to satisfy the following recognition criteria at that date however:

- In cases where an asset other than an intangible asset, is likely to be associated with future economic benefits for the acquirer and its fair value can be measured reliably;

- In cases where a liability other than a contingent liability, is likely to lead to an outflow of resources and where representative economic benefits will be required to settle the obligation. Its fair value must be able to be measured reliably; and finally

- In cases where the fair values of an intangible asset or a contingent liability can be measured reliable.

Furthermore, IFRS 3 requires the identifiable assets, liabilities and contingent liabilities, which satisfy the recognition criteria above, to be measured initially by the acquirer at their fair values at the acquisition date, irrespective of the extent of any minority interest.

IFRS 3 requires the acquirer to re-examine the identification and measurement of the acquired company's identifiable assets, liabilities and contingent liabilities and the measurement of the cost of the business combination if the acquirer's interest in the net fair value of the items recognised exceeds the cost of the combination. Any excess remaining after that reassessment must be recognised by the acquirer immediately in profit or loss.

(IASCF, 2004; KPMG, 2004)

Goodwill
IFRS 3 requires goodwill acquired in a business combination to be recognised by the acquirer as an asset from the acquisition date. Goodwill is measured as the excess of the cost of the business combination over the acquirer's interest in the net fair value of the acquired company's identifiable assets, liabilities and contingent liabilities. (IASCF, 2004; KPMG, 2004)

The amortization of goodwill acquired in a business combination is now prohibited and instead it requires the goodwill to be tested annually for impairment, or more frequently if events or changes in circumstances indicate that the asset might be impaired, in accordance with IAS 36 *Impairment of Assets*. Previously recognized goodwill should discontinue to be amortized. (IASCF, 2004; KPMG, 2004)

Intangible Assets

When it comes to the intangible assets they are accounted for in an acquisition according to IAS 38 if they fill the definition of intangible assets and if the fair value can be measured reliable. In order to be categorized as an intangible asset the definition states that it has to be identifiable, in control by the company, and expected to bring economic benefits to the company. Hence, it should be identified separately from goodwill. This implies, for example, that some research and development projects in the acquired firm should be accounted for as a separate intangible asset in the consolidated balance sheet. (IASCF, 2004; Deloitte, 2005)

Impairment test of assets

IAS 36 *Impairment of assets* requires the recoverable amount of an asset to be measured whenever there is an indication of impairment. There is also a requirement that impairment is tested annually for intangible assets with indefinite useful lives, intangible assets not yet available for use, and for goodwill acquired in a business combination. An impairment loss is incurred when the assets carrying amount exceeds its recoverable amount. An assets recoverable amount is the highest of the value in use and the fair value less costs to sell. Value in use is the present value of the future cash flows that is expected to be derived from the asset. Fair value less costs to sell is the amount attainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the cost of disposal. (IASCF, 2004; Deloitte, 2004)

Disclosure

IFRS 3 requires disclosure of information that enables users of an entity's financial statements to evaluate the nature and financial effect of business combinations that were affected during the period; business combinations that were affected after the balance sheet date but before the financial statements are authorised for issue; and some business combinations that were affected in previous periods. Primarily it requires disclosure of information that enables users of an entity's financial statements to evaluate changes in the carrying amount of goodwill during the period. (IASCF, 2004; KPMG, 2004)

2.3.7 Main differences between IFRS 3 and the former Swedish accounting rules

There are some essential differences between IFRS 3 and the former Swedish rules on consolidation RR 1:00. In order to describe this distinction the following points gives an illustration of the most important changes that came along with IFRS 3 and these are:

1. Under IFRS 3, all acquisitions will be accounted for by the purchase method. Hence, the pooling method is no longer allowed.

2. The acquirer will under the new rules have to take up all the acquired assets, liabilities and contingent liabilities to its fair value. This implies that even an eventual minority interest in the acquired company should be accounted for by its fair value. The earlier rules in RR 1:00 stated that only a proportional part of the acquired firm's net assets could be valued by fair values. This rule is no longer allowed in IFRS 3. IFRS 3 is also demanding that identifiable intangible assets are accounted for as separate assets in the balance sheet and not as a part of goodwill which was possible earlier.

3. Goodwill is no longer subject to amortization under the new rules. Instead the value of goodwill will be subject to a yearly impairment test according to the rules in IAS 36.

4. Dismissals for restructuring costs can only be accounted for if there, at the acquisition date, exists obligations at the acquired firm and that it fulfils the requirements in IAS 37. According to IAS 37, a dismissal for restructuring can further only be accounted for when there exists a detailed and announced restructuring plan that are approved by all the affected parts.

5. The demand for disclosure of information has been expanded substantially under IFRS 3 than under earlier Swedish rules and norms.

(Deloitte, 2004)

2.4 Previous Studies on Accounting Standards impact on Acquisitions

Since IFRS 3 was first introduced in January 2005 the affect it has on corporations have not yet been fully examined. However the authors have found a number of articles and surveys that have studied the potential affects of IFRS 3 on corporation and on acquisitions in particular.

According to KPMG (2003), IFRS 3 for business combinations could have a significant implication for companies in all industries because increased transparency and comparability could lead to greater consolidation within and across borders. Furthermore, impairment charges will have a direct impact on a company's earnings-based valuation metrics, and an increased amortization of assets under current purchase accounting rules could make business combinations appear less attractive. Finally, non-amortization of goodwill through IFRS 3 could make business combinations appear more attractive.

Additionally, PricewaterhouseCoopers (2004) states that results will be harder to predict due to more frequent, comprehensive and rigorous impairment testing of acquired assets. Furthermore, greater analysis is needed on the target entity's business in advance of a transaction in order to be able to identify potential intangible assets and to determine the risk of impairment changes.

The financial statements will look very differently following an acquisition. The recognition and measurement requirements will make it harder to demonstrate earnings uplift from the acquisition as more of the acquisition's costs will have to be expensed as they are incurred. (PricewaterhouseCoopers, 2004)

Moreover, IFRS 3 will, according to Jansson, Nilsson & Rynell (2004), give rules that imply that companies will not need to execute the almost impossible task of estimating useful life regarding goodwill any longer. Jansson et al (2004) further states that on the other hand will the requirement of a yearly valuation of goodwill bring additional work and substantially increased demand of information for the companies.

The major benefit by amortization of the goodwill evenly is that it is possible with a greater accuracy to predict the impacts of earnings. (Stevenson & Mcphee, 2005)

To summarize, the previous studies of the effects of IFRS 3 on acquisitions, the acquisition process should become more rigorous, from planning to execution. More rigorous evaluation of targets and structuring of deals will be required, in order to withstand greater market scrutiny. Expert valuation assistance may be needed to establish values for items such as new intangible assets and contingent liabilities. (PricewaterhouseCoopers, 2004)

3 Methodology

This chapter will describe the procedure used to conduct the empirical research. This includes how the data was collected, determination of the sample used and how the information will be interpreted. The chapter ends with a discussion on the reliability and validity of the chosen methods.

3.1 Research Method

Before the research can start, the researcher must determine the aim of the study. Does it aim at confirming/rejecting existing theories by applying them to new observations made, or does it aim at deriving new explanations and theories from existing observations? The different approaches are called the deductive and inductive method (Halpern, 2003).

In the deductive method, you begin with a hypothesis that you believe to be true and then make systematic observations to see if your hypothesis is correct (Halpern, 2003). It focus on pre-existing formulas or theories which then is applied to observations made in the real world and thereby tries to explain the world through the pre understood theories. These hypotheses can then be proven right or wrong by using empirical studies. (Holme & Solvang, 1991) The deductive method is sometimes described as "going from the general to the specific" (Halpern, 2003).

In the inductive method, you observe events and then devise a hypothesis about the events you observed (Halpern, 2003). It focuses on the observations made of the world and a specific occurrence and tries to work out a formula explaining the observations. The specific observation is made into a generalization about the world (Losee, 2001). When one reason inductively, one generalize from experiences to create beliefs or expectations. The inductive method is sometimes described as "going from the specific to the general." (Halpern, 2003).

In this thesis the authors are taking an inductive approach. This since empirical observations will be gathered from a specific occurrence, i.e. the introduction of the new accounting standards. Once this is done the authors will with the aid of the theoretical framework explain and analyze the findings in order to come to a general conclusion of how the new standards have influenced financial statements and acquisitions processes of listed Swedish companies. Hence, the inductive approach will be used for this thesis.

3.2 Quantitative and qualitative research approach

Business research is defined by Zikmund (2000, pg 5) as "*the systematic and objective process of gathering, recording and analyzing data for aid in making business decisions*".

The philosophy of information gathering has concluded two different ways to gather and analyze research data and information. The two perspectives are named the qualitative and quantitative method. The two methods are, because they gather information differently, also used differently in research. Since the authors of this thesis will use both approaches, a more thoroughly discussion of the two will follow below.

The quantitative approach bases information gathering on an objective base, which means that the researcher should be positioned far away and observe the information and not be a part of it, in order to be as neutral as possible (Holme & Solvang, 1991). The purpose of quantitative research is to determine the quantity or the level of some phenomenon in the form of numbers (Zikmund, 2000). In order to be as neutral as possible, using a random sample from the whole population will be desirable, and from that state a conclusion which can be assumed true for the general population as well. This method will lead to a conclusion of a more general type. In this kind of approach statistics is often used in order to prove hypothesis about the population sample (Ejvegård, 1993).

Since the authors, through the first research question of this thesis, aim to get insights of the balance sheets and income statements of the companies a quantitative method will be applied for this special element. This method will be used because it includes numbers, which makes it possible to gather information more objectively and it allows the authors to state a conclusion which can be assumed true for the general population.

The focus of the qualitative approach is not on numbers but on words and observations; visual portrayals, narratives, meaningful characteristics, elucidation, interpretation and other expressive descriptions. Any source of information may be informally examined to clarify which qualities of characteristics that is associated with an object, phenomenon, situation and issue. The qualitative approach is dominantly used when the researcher wants to have a deeper understanding of a problem (Zikmund, 2000). The qualitative method is using information where the source has had a great degree of freedom in outlining its own opinion. Gathering the information this way will give information about a certain and detailed problem and is normally conducted during normal conversations, surveys or interviews. The data will also be very specific and apply only to that particular research question. (Holme & Solvang, 1991) Furthermore, in a qualitative study the researcher use a smaller sample to be able to make a conclusion of the research question (Saunders, Lewis & Thornhill, 2003).

In the second research question the authors are examining the companies view on the accounting change, which means that the source will have the possibility to outline its own opinion. The authors have therefore chosen the qualitative research method for this part in order to gather a deeper understanding of the problem and also because the data will be very specific and therefore it can probably only be applied to this particular research. The qualitative research will be conducted in the form of a survey.

3.3 Methodological triangulation

Triangulation refers to the use of more than one approach when it comes to investigation of a research question in order to improve confidence in the resulting findings. Since much of the research within all kinds of fields is founded on the use of a single research method and as such may suffer from limitations associated with that special method or from the specific application of it, triangulation will offer the prospect of improved confidence. (Bryman, 2003) Triangulation is a method used by qualitative researchers to check and establish validity in their studies (Guion, 2002).

Methodological triangulation involves the use of multiple qualitative and/or quantitative methods. If the conclusions from each of the methods are similar, validity is established. Guion (2002) gives in a study the following example of a situation where a methodological triangulation might be useful: suppose you are a manager conducting a case study of one of your employees to document changes in his/her life as a result of participating in an on-the-job training program over a one- year period. You would not just use one method, but you would use interviewing, observation, document analysis, or any other appropriate method to assess the changes. If the findings from all the methods draw the same or similar conclusions, then validity has been established in the research. However, this method may require more resources in order to evaluate the data and research using different methods. Likewise, it will be more time consuming when it comes to analyzing the data/information yielded by the different methods. Hence, the more validity wanted the more time consuming the research will be. (Guion, 2002)

Even if a triangular strategy not can be seen as a completely quick fix for certifying validity it will improve the validity (Marschaan-Piekkari & Welch, 2004).

By looking at the purpose of this thesis "*How IFRS 3 affect the companies listed on the Stockholm Stock Exchange and its impact on the acquisition practices*"; the authors can primarily conclude that a qualitative research method will best fulfill this purpose. However, in order to get a holistic view of the impact of the new accounting standards a quantitative research is also needed in order to identify the changes in the companies' financial statements. Hence, the qualitative method will be used for the survey and the quantitative method will be used for the observation of the balance sheets and the income statements of the companies. This is the process of methodological triangulation and the researchers have chosen this method in order to improve the confidence of the thesis. The authors are also confident in that, by using the methodological triangulation method, greater insights can be made of the organizational effects of IFRS 3, IAS 36 & IAS 38.

3.4 Primary and Secondary data

In the field of methodological research, the collected data can be classified into two separate groups, primary-and secondary data. They differ in their closeness to the question being researched. Primary data is collected specifically for the proposed research question, usually through interviews or questionnaires, while secondary data is already existing data that has been collected for other purposes. (Saunders, Lewis & Thornhill, 2003)

The advantage of using primary data is that the researcher can adjust the collected data based on the details of the research question. The main reasons to use secondary data are that it is cheaper and faster to collect than primary data (Saunders, Lewis & Thornhill, 2003). There are two types of secondary data, raw- and compiled data. Raw data is data where there has been little, if any, processing, while compiled data is data that have received some form of selection and processing (Kervin, 1999).

In this thesis the authors will be using both primary-and secondary data. For the first research question, the authors will look in companies annual reports and extract the figures needed to answer the question. This means that compiled secondary data is used, this since the numbers are collected and presented for other purposes than this thesis and furthermore, that the numbers presented in the annual reports are selected and processed by the company before printed in the annual report. The authors will look at a wide range of numbers in the annual reports, both in the balance sheet and in the income statement this in order to identify the impact of the new accounting standards. Since this thesis does not take taxes into consideration, the operating profit[5] will be used when examining the companies' earnings in the income statement. Furthermore, since two of the companies are using Euros (€) as their reporting currency, the authors have needed to re-calculate these entries into Swedish kronor (SEK). This was done by using the average monthly exchange

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[5] Profits before deduction of interests payments and income taxes. Also called Earnings before interest and tax, EBIT. (Investorwords, 2006)

rates from the Swedish tax authority (Skatteverket, 2006). The monthly rates where added together and then divided by twelve in order the get the year's average exchange rate. This measure has been chosen since the authors believe that it will best capture the fairest exchange rate during the year.

For the second research question primary data will be used. This since the authors will use surveys that will be answered by corporate managers and where the authors can design, formulate and present the specific questions in order to collect the information needed to complete the purpose of this thesis.

3.5 Surveys

As already mentioned in section 3.3 a survey will be used to conduct the qualitative research. A survey is according to Zikmund, (2000, pg 167) "*a research technique in which information is gathered from a sample of people by use of a questionnaire; a method of data collection based on communication with a representative sample of individuals*". Hence, a survey can be seen as a method of primary data compilation based on communication with a representative sample of individuals.

Surveys can be conducted through mail, e-mail, telephone, internet or face-to-face interview. The dominant technique when it comes to accounting and finance research is mail surveys and e-mail surveys. (Smith, 2003)

Surveys require asking people, who are referred to as respondents, for information by using either verbal or written questioning. The type of information collected in surveys varies significantly from time to time, depending on the objectives of the survey. Normally, survey studies attempt to give a description of what is happening or to learn the motives for a particular business activity. Hence, most survey research is descriptive research but they can also be designed to provide casual explanations or to explore ideas. Some of the typical survey objectives include to locate characteristics of a particular group, measure attitudes, and to describe behavioral patterns. (Zikmund, 2000)

The advantages of surveys are that they provide inexpensive, quick, efficient ways of assessing information about a population (Zikmund, 2000). Other advantages associated with this kind of technique are that it can reach a lot of respondents and that everyone receives the same questions. The disadvantages of surveys are the possible reduction of respondents and the respondents varying interpretations of the survey (Kylén, 1994)

The reasons for choosing a survey-based approach instead of an interview-based for example, are that it is possible to reach a broader range of respondents than otherwise and that every respondent will receive the same questions. Thus, in this thesis, with the help of a survey, it is possible to reach an additional proportion of companies that will get the chance to respond to the same questions and this can be done in a relatively short time.

3.5.1 Questions in a survey

In most surveys the first question is to identify the recipient of the survey. This is done in order to make sure that the individual responding to the survey possesses the characteristics wanted and therefore is eligible to so. (Brace, 2004) In this thesis the authors are looking for accounting managers or chief financial officers that have knowledge of the accounting standards and are informed on the company's acquisition process. This is done by obtaining the relevant e-mail addresses from the company's websites or by sending an e-mail to the investor relation department with a request of forwarding the survey to the wanted person.

3.5.2 Designing the Questions

A main rule when it comes to questionnaires is according to Brace (2004) to start with questions of a more general nature and then narrow it down to the specific, more detailed, questions. This since respondents might find it difficult to answer questions about details, and by starting with general questions the respondent can ease into the subject before reaching for specific details. It is of crucial importance that the questions in the survey have a clear link between them and that it flows naturally from one subject to another (Brace, 2004; Kýlen, 1994). Furthermore, Brace (2004) states that different types of questions are appropriate for different purposes. The survey writer should be thinking of how the questions will be analyzed before writing them, this in order to design them appropriately.

Survey questions can be designed in many different ways. For example, they can be opened-or closed questions. An open question[6] is one where the range of possible answers is not suggested in the question and where the respondent is free to formulate his/her own opinions and freely express his/her thoughts. The open questions have advantages in that they can retrieve much information and that each respondent is free to express his/her precise opinion. However, there are also shortcomings to this method. The respondent may find it difficult to recognize and articulate their opinion in the specific matter. Closed questions, on the other hand, are questions where there are a limited number of answers that the respondent can give. For example, a yes or no question is a typical closed question. (Brace, 2004; Kýlen, 1994)

In this thesis open questions will be used in order to conduct the survey. These questions will be used since the respondents will likely have different opinions on how the new accounting standards effect their company and therefore the authors does not know the range of answers to the proposed questions. Moreover the authors aim at gathering opinions from the respondents that are not limited by the nature of the questions and thus open questions will most likely fulfil this aim.

The actual survey[7] starts with questions of the more general genre and identifies the respondent's position and number of years at that position. The rest of the survey is divided into four parts (goodwill, valuation of acquisition candidates, intangible assets and other aspects) where each part consists of three to four questions. The authors have limited the number of questions in order to thereby decrease the time needed for the respondents to complete the survey and thus increase the response rate. Furthermore, by using a limited number of questions the authors expect to receive more extensive answers for each question from the respondents. To further increase the response rate the authors have designed the questions in an interesting, structured and straightforward way, using a language that is comprehensible.

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[6]Also known as unstructured or free-response questions (Brace, 2004).

[7] The complete survey can be found in the appendix

3.6 Sampling design

Having defined the research objectives, the research approach and the data collection method the next stage of the process is to specify the sampling design. The sampling design specification defines the sampling frame to be used in the survey, the methods used for randomly selecting the sample from the frame, and the size of the sample. (Biemer & Lyberg, 2003)

A major part in the process of making surveys useful is the way of handling sampling. Sampling is the process of how to select a small subset of a population[8] parameter out of the whole population. The key to useful sampling is to find a way of giving everyone or almost everyone in the population the same chance of being selected. How well a sample represents a whole population depends on the sample frame, the sample size and of the particular design of the selection process. (Fowler, 2002)

3.6.1 Sampling frame

Every sampling process will give some individuals a chance to be included in the sample while excluding others. The first step in evaluating the quality of the sample is to define the sample frame. (Fowler, 2002)

The people that will get the chance of being included among those selected constitute the sample frame (Fowler, 2002). This means that the sampling frame can be said to be the collection of target population members from which the sample can be drawn. It can also be a combination of lists and other kinds of devices that can be used to select a sample. (Biemer & Lyberg, 2003)

In order to create a sample frame the researcher therefore needs to ask the question of who is to be sampled. In this thesis the authors have chosen to use a sampling frame including Swedish companies quoted on the A-list and the O-list's *Attract 40* at the Stockholm Stock exchange. The reasons for choosing companies on these lists are that they are larger, have higher turnover and are involved more often in acquisitions than companies on the other lists. Shortly, larger companies have a higher probability of being involved in acquisitions and are therefore more influenced by the new accounting rules on business combinations.

3.6.2 Random sampling and sample size

When decisions regarding the sample frame have been made, the next question is how to select the individual elements to be included in the study and how many elements to include. Random sampling is the prototype of population sampling and can be illustrated by taking a sample out of a hat where members of a population are selected one at a time, independent of each other and without replacements. When a member of the population has been selected it has no further chance to be selected again. When it comes to the decision of sample size there is rarely a definite answer of how large it should be for a given study. It is important though that the sample size is large enough in order to address the objectives of the study. (Fowler, 2002)

In this thesis the authors have as already stated, chosen to only include companies quoted on the A-list and the O-list's *Attract 40* at the Stockholm Stock exchange. The companies

[8] A complete group of entities that share some common set of characteristics. (Zikmund, 2000)

on these lists, which constitute the sample frame, consist of 114 companies in total. Out of these companies the authors have conducted a random sample procedure in order to limit the amount of companies used in the research. This has been done by using the function *exactly* in the statistical computer software SPSS. By using this method the authors have been able to limit the sample of companies studied and also been able to avoid some possible bias. The authors have chosen to limit the sample of firms in the study to 30.

It can be argued that a larger sample would be better since the larger the sample the greater is the reliability of the statistical analysis. The reason for this is that the sampling error is minimized by increasing the number of observations. (Bryman & Bell, 2003; Cooper & Schindler, 2001). However, by using a sample of 30, according to statistics, one can assume that the sample will follow a normal standard distribution and hence, is an appropriate number in order to identify reasonable conclusions about the population as a whole (Aczel & Sounderpandian, 2002). The authors are confident that this sample is large enough in order to address the objectives of the thesis.

Out of these 30 companies 3 were using US GAAP[9]. Since these companies do not apply the international accounting standards they are not included in the study. Through a new random sample the authors selected 3 new companies; hence the total sample for the quantitative study is 30 companies[10].

From this sample the authors have further divided the sample into seven groups[11] depending on their line of business. These groups of industries have been formed based on the authors' knowledge of the companies and their industry. After this the sample consists of nine companies within the industrial segment, three companies within construction and real estate, four companies in the raw material segment, five companies within IT and telecom, two companies in the security segment, four companies in the bank and investment segment and finally, three companies are grouped together in a segment called *other*. In the *other* segment companies from media, healthcare and consumer goods are grouped together since they did not belong to any of the defined industries. The reason for grouping companies together depending on their industry is that the authors wish to examine if the new accounting standards have affected the industries differently. This is not the primary aim of the research, but will function as a supplement to the main research.

The random sampling method has been used for both the quantitative and the qualitative research which means that the same number of companies have been chosen for both the research methods. The difference between them though is that in a survey there might be a possibility of nonresponse and bias (see section 3.7).

3.7 Possible errors in surveys

Surveys are as already mentioned based on asking respondents for answers. If these people collaborate and give reliable answers, the survey will hopefully accomplish its goals. There are however two basic disadvantages of surveys that occur if these conditions are not met: Nonresponse error and response bias. (Zikmund, 2000)

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[9] United States Generally Accepted Accounting Principles

[10] A list of the companies included in the sample can be found in Appendix II

[11] See Appendix III

Nonresponse error is the statistical difference between a survey that includes only those who answered and a survey that also included those who failed to answer. There are very few surveys that have 100 per cent response rate and the problem of non-respondents is especially occurring in mail surveys. (Zikmund, 2000)

There are however a lot of methods available in order to reduce nonresponse in surveys. Fowler, (2002) states that in order to reduce nonresponse the layout of the survey should be clear, the questions should be attractively spaced and the response tasks should be easy to do for the respondent. Fowler, (2002) further conclude that it is important to send the surveys to the right people, give detailed instructions of how to answer the surveys, give respondents the ability to be anonymous and then send reminders to respondents that have not answered. Moreover, the survey should be interesting and rewarding for the respondents (Kylén, 1994).

Another possible error connected to surveys is response bias. Response bias is a type of statistical bias which can affect the result of a survey. It is present when the respondents tend to answer in a certain direction, i.e. instead of answering truly honest give the answer which they think the researcher wants them to answer. This is usually seen in studies where the researcher is looking for a certain answer and therefore asks leading questions. (Zikmund, 2000)

In order to avoid these possible errors the authors have in this thesis put a lot of effort in creating a clear survey with understandable and straightforward questions for the respondents. In order to send the survey to the right people and to receive many responses the authors have sent e-mails mainly to the investor-relations managers of the companies. In this e-mail contacts were made with the people in the right positions within the company. The authors have also tried to design the letterhead as appropriate as possible, giving the respondents all the needed instructions in order to fill in the survey. Since the information asked for, from the companies, can be of the confidential genre the respondents have therefore also been able to be completely anonymous and this will most likely reduce nonresponse and bias. To increase response rates reminder e-mails have also been sent to the companies not responding after the initial deadline.

As already concluded some important actions have been taken in order to adjust and reduce the nonresponse bias of the surveys. Despite these actions and the efforts to minimize nonresponse, less than 100 per cent will usually respond to a survey and typically the response is considerably less (Biemer & Lyberg, 2003). The research in this thesis will be conducted through both a quantitative and a qualitative research method (see section 3.3.). The problems connected to nonresponse and response bias will only be present in the qualitative research (Brace, 2004). However, the fact that nonresponse will most likely be present does not affect the thesis considerably. This since open questions are used for the survey and the main goal of these questions is not to receive as many answers as possible but merely to gather answers of high quality (Saunders et. al 2003). This implies that the responses received for the qualitative part do not need to be 30, instead the authors opinion is that approximately 10 responses are considered enough if the answers are of high quality. To further validate a smaller sample for the qualitative part, the fact that through the quantitative research a determined sample of 30 companies are used and therefore the authors have gain knowledge of how the new accounting standard IFRS 3 has affected the companies. Since this research is conducted before the qualitative research the authors are confident in that, even if there exist nonresponse in the qualitative part, conclusions can still be drawn of the general genre.

3.8 Validity and Reliability

When conducting a study it is hard to be truly objective as a writer. However, it is of crucial importance to stay as objective as possible in order to report a trustworthy result. This is accomplished through the use of relevant data within the subject, a neutral approach in the analysis of data, logical conclusions and equilibrium between dissimilar interests on the subject studied (Eriksson & Wiedersheim-Paul, 2001). The authors of this thesis have stayed as objective as possible but are aware that some possible errors can occur. In the methodology literature several possible errors that can occur within a thesis are mentioned but the most important are the ones of low validity and low reliability (Zikmund, 2000).

3.8.1 Validity

Validity deals with whether the conclusions drawn from the data are valid, i.e. the ability of the researchers to measure what is intended to be measure (Bryman & Bell 2003). If the study does not measure what was planned, there is a dilemma. Researchers want to know if their measure is valid, and the question of validity explains their apprehension with correct measurement (Zikmund, 2000). It is an obligation for all researchers to conduct thorough studies, regardless of their research practice. The process of validating studies based on qualitative research strategies is therefore a core issue for both the readers and creators of qualitative data (Marschaan-Piekkari & Welch, 2004).

In order to increase the validity of this thesis the authors have, as described earlier, used the methodological triangulation approach. The research of Marschaan-Piekkari & Welch (2004) and Guion (2002) clarifies that the use of this method will lead to improved validity. These findings have been captured and the authors are confident that by using both a qualitative and quantitative approach more validity will be established which will add confidence to this thesis.

Moreover, since the sources of information used are primary data retrieved directly from the companies and secondary data presented in annual reports the information is considered reliable. This in view of the fact that the annual reports are controlled by legislations and therefore have high credibility.

3.8.2 Reliability

Reliability tells us whether a result is replicable or not and is the degree to which a measure is free from errors and thus will yield consistent results (Bryman & Bell 2003). Reliability applies to a measure when comparable results are achieved over time and across situations. (Marschaan-Piekkari & Welch, 2004) In the case of surveys, reliability is the extent to which the result is replicable if performed again. Daymond and Holloway (2002) states that since the researcher of qualitative survey is the main research instrument and therefore the result would not be fully replicable if performed by another researcher. This is due to the fact that background and personal characteristics influence the research and by that also the final result. To limit the possibility of low reliability based on choices and selections made by the authors, all the data, methods and decisions made during the making of this thesis has been recorded in order to be able to re-evaluate the process and to locate possible errors.

Furthermore, one can argue that using a sample size of 30 is too low in order to ensure reliability of the research. However, according to Buglear (2005) the previously mentioned idea that the larger sample the better, does not necessarily has to be true. Buglear states that the larger the sample you have, the less is the marginal advantage per increase in sample size. By using a sample of 30 observations implies that the standard normal distribution can be used in any statistical decision-making and that the sample does not have to come from the normal population (Buglear, 2005; Aczel & Sounderpandian, 2002). Hence, the authors are confident that a sample of 30 will fulfill the purpose and combined with the methodological triangulation add validity and reliability to the thesis.

Furthermore, as already mentioned in section 3.7, there are some errors that can exist in a survey and this can most certainly reduce the reliability of the research. The more errors the less is the reliability. However, in order to improve the reliability and reduce errors the authors have been putting effort in creating a clear survey with understandable and logical questions for the respondents. The authors have also put effort in sending the surveys to the right people, within the companies, that possesses the right knowledge in order to answer the survey. Furthermore, have the respondents been given anonymity in order to get trustworthy answers. These steps regarding the survey have most certainly led to improved reliability since possible errors are reduced.

4 Empirical Findings and Analysis

In this part, the empirical findings will be presented followed by the authors' analysis of the different sections. The chapter starts with a presentation of the findings of the quantitative- and the qualitatative research. Each section will end by a thoroughly analysis in order to give the reader a straightforward connection to the empirical part. Each section will create a foundation for answering the purpose of this thesis of how the new accounting standards IFRS 3 have affected the financial statements and acquisition practices of companies.

4.1 IFRS 3, IAS 36 and IAS 38´s effects on the financial statements

To be able to answer the first research question, of how the new accounting standards IFRS 3 *Business Combinations*, IAS 36 *Impairment of Assets* and IAS 38 *Intangible Assets* have affected the financial statements of the companies, the authors have gathered and analyzed information from the annual reports of a random sample of 30 companies[12]. In order to make comparisons and to draw confident conclusions annual reports from both 2004 and 2005 have been used.

The effects on the financial statements of the companies are presented both as a total and also divided into industries (see section 3.6.2). All figures and calculations presented in this section can be found in Appendix III.

4.1.1 Effects on the income statement

By studying the financial statements of the 30 companies it became clear that the new accounting standards have had a great impact on the companies operating profits. The combined operating profit of the 30 companies in the study was 135 billion SEK in 2004 and as can be seen in figure 2, 9.54 per cent or 12.9 billion SEK of these profits were due to IFRS 3, IAS 36 and IAS 38.

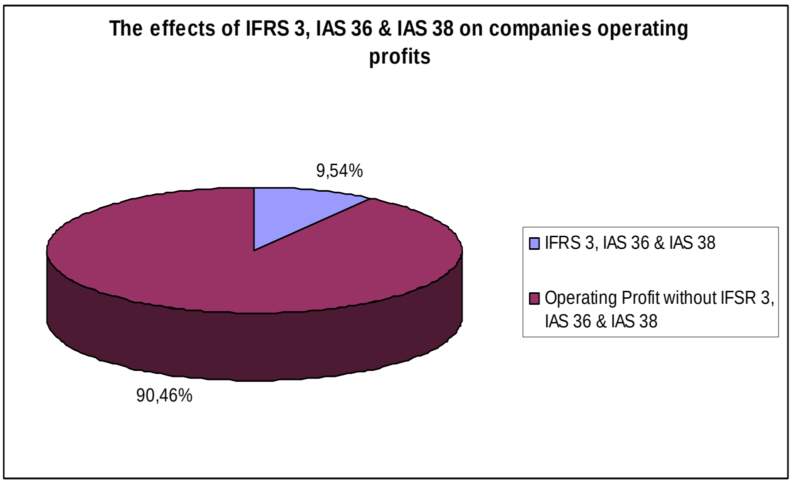

Figure 2 The effects of IFRS 3, IAS 36 & IAS 38 on companies operating profit

[12] See Appendix II

Furthermore, the authors found that the influence of the new accounting standards differed depending on the line of business. As figure 3 shows, the percentage change in operating profit due to the implementation of IFRS 3, IAS 36 & IAS 38 ranged from 4.94 per cent, for the bank and investment segment, and up to 24.00 per cent for the security segment.

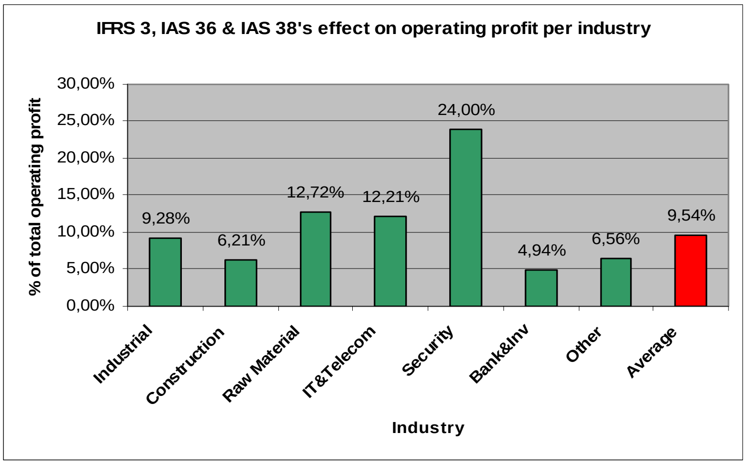

Figure 3 IFRS 3, IAS 36 & IAS 38's effect on operating profit per industry

A large factor in the security segment is the multinational company Securitas whose operating profit increased with 26.3 per cent due to the new accounting standards. In the industry with the most number of companies in the study, the industrial segment, the effects of the accounting standards were close to the average with an increase in operating profit of 9.28 per cent (figure 3). In the other industries the effects of the accounting change varied from 6.21 per cent to 12.72 per cent.

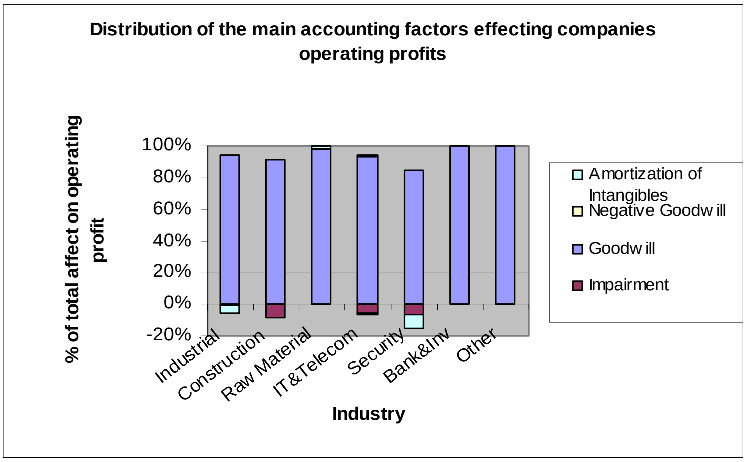

Figure 4 Distribution of the main accounting factors effecting companies operating profit

In figure 4 above, the distribution of the effects that the new accounting standards have had on companies operating profits are illustrated.

By looking at figure 4, one can see that goodwill represented the major impact on the change in companies operating profits in all industries. Goodwill has had the least impact in companies in the security industry. However, the goodwill effect in this industry still resulted in around 85 per cent of the impact on the total change in operating profits derived from the change in accounting standards. The new rules on goodwill have had the most significant effect on profits in the industry categorized as other and in the bank and investment industry. In these industries, the goodwill entry stood for the whole change in profits, derived from IFRS 3, IAS 36 & IAS 38. The figure also shows some negative impact which appeared because of amortization of intangibles and impairment of assets. These effects appeared in the industrial, construction, IT and telecom, and the security industries. The negative impacts were however totally overshadowed by the positive impact that the new accounting rules have had on the operating profits.

4.1.2 Effect on the companies' balance sheets

Figure 5 below, illustrates the distribution of the new accounting factors affecting the companies balance sheets. As in the income statement the new rules on goodwill have had the biggest impact also on the balance sheet.

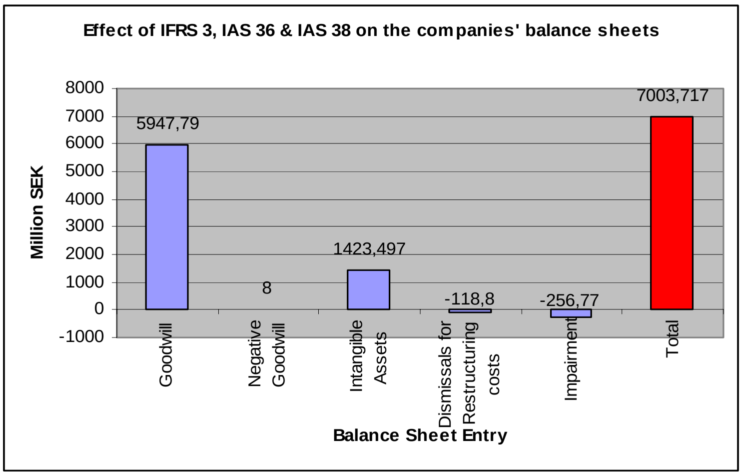

Figure 5 IFRS 3, IAS 36 & IAS 38's effect on the companies' balance sheets

The total effect on the balance sheets for the 30 companies was an increase of approximately 7 billion SEK. This increase was evident on both the asset and respectively the owners' equity side of the balance sheet.

By looking at figure 6 below, one can see the distributional effects of the new accounting factors in the companies' balance sheets.

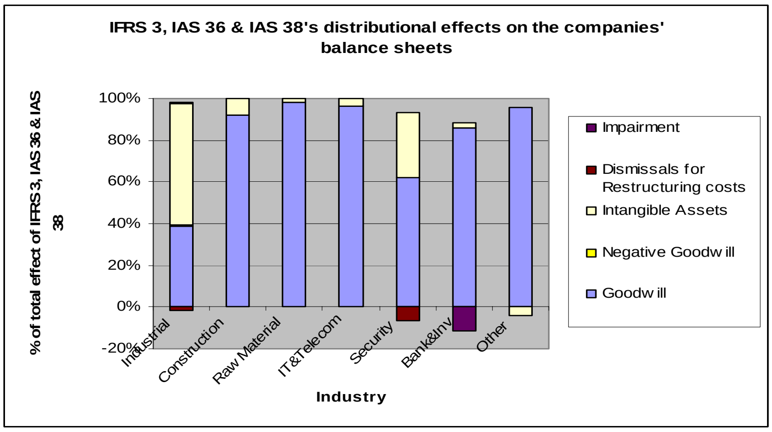

Figure 6 IFRS 3, IAS 36 & IAS 38's distributional effects on the companies' balance sheets

The impact of goodwill was especially high in companies belonging to industries categorized as other, construction, raw material, IT and telecom and to the bank and investment industry. The increase in the assets and respectively in owners equity in these industries were to a large extent dependent on the goodwill entry which accounted for 80-99 per cent of the total change in the balance sheet. From figure 6, one can also see that every industry but other has had positive effects from intangible assets. The industrial and the security industry differed from the others since they showed significantly higher effect from intangible assets. Out of the total change in the balance sheets around 60 per cent were a result from intangible assets in the industrial industry and the change in the security industry was 30 per cent. Dismissals for restructuring costs have, as seen in the figure, affected the companies in a negative way. The negative effects were evident in the industrial and security industries. Furthermore, impairment affected the balance sheet negatively in the bank and investment segment and in the industrial segment.

4.2 Analysis of IFRS 3, IAS 36 & IAS 38's effect on financial statements

As seen in figure 4, goodwill represented the major impact of the change in accounting standards. As Tempte (2005) states, amortization is an expense and therefore it effect the income statement negatively. Now, through IFRS 3 *business combinations*, goodwill can no longer be amortizised, which has led to increased profits. Amortization of intangibles (IAS 38) and impairment of assets (IAS 36) are expenses that effect the income statement negatively, which is natural since the value of the asset therefore has decreased. The fact that profits has increased implies that the companies have found no reason to impair their goodwill, or when impairment has been justified it has been less than the amortization.

As figure 2 shows, the average increase in operating profit, due to the new accounting rules, was 9.54 per cent for the 30 companies. This finding is in line with Rogneruds (2006) and Sunesons (2005) articles where they, separate from each other, came to the conclusion that 8 - 10 per cent of the listed companies' earnings where due to the accounting change. By looking at figure 3, the authors can conclude that IFRS 3, IAS 36 & IAS 38 affects all industries in a similar way. This is in line with a study made by KPMG (2003) which states that IFRS 3 could have an impact on companies in all industries because of transparency and comparability. It was only the security segment that was significantly different from the others (15 per cent above average). This was mainly due to Securitas exceptionally large goodwill entry (due to many acquisitions) that under the new accounting standards no longer could be amortizised and therefore had to be reversed, creating a large positive effect on operating profit.

By studying the companies balance sheets one can conclude that goodwill and intangible assets has increased the assets and the owners' equity, while dismissals for restructuring costs and impairment has decreased the assets and owners' equity (see figure 5). The goodwill entry has had the largest impact of the new accounting standards on the assets and owners' equity. As for the income statement this change derives from the fact that, under IFRS 3, goodwill no longer can be amortizised which implies that the asset side increases when the non-amortization effect over-shadows the impairment effect.

Since the fundamental idea of a balance sheet is that the assets should be balanced by the companies' equity and liabilities, the new accounting standards must have an effect on both sides (Tempte, 2005). As IFRS 3 prohibits the amortization of goodwill, it is therefore no longer an expense in the income statement and is thus, added to the assets of the balance sheet. As the authors have already concluded, IFRS 3 also increased the companies' profits and since profits are a part of owners' equity this has also increased.

Next after the goodwill entry, intangible assets have changed the most. This is mainly due to the fact that companies must now account for intangible assets separately and not as a part of goodwill. As figure 6 shows, especially the industrial and security segment has increased the intangible assets entry in their balance sheets. This implies that these industries used to have large amounts of intangible assets included in the goodwill entry and that they have been able to re-classify the intangible assets and hence, account for them separately in the balance sheet.

The new rules regarding dismissal for restructuring costs has as seen in figure 6 effected a few companies' balance sheets in a negative way. This stems from the fact that dismissals for restructuring costs can only be accounted for if there at the acquisition date exists obligations at the acquired firm (Deloitte, 2004). Companies experiencing these negative effects have most likely not been able to demonstrate that an obligation exists in the target company and they have therefore been required to expense the restructuring costs immediately. However, the effects of these dismissals have not affected the companies significantly.

4.3 The companies view on the affects of the new accounting standards

The qualitative research was performed by using a survey (see appendix 1). This survey was sent to the same 30 companies used in the quantitative research. The response rate for the qualitative research was 50 per cent, meaning that 15 companies of the 30 responded to the survey. The reason for the relatively low response is that the spring period, when this thesis is written, is according to the companies an exceptionally hectic period. This since annual reports as well as the reports for quarter 1 is due, creating a heavy work burden for the targeted respondents. However, since the primary aim of the qualitative research was not necessarily to get a high response rate, but merely to get high quality answers, the authors believe that the responses received is sufficient to answer the research question.

Since most companies in the study wishes to be anonymous no companies will be named for this part of the research. To be able to present the respondents answers in a comprehensible way, the authors have chosen to divide the questions into four different parts, "Goodwill", "Valuation of acquisition candidates", "Intangible assets" and "Other aspects". These parts follow the sequence of the survey. The answers presented in this part are a summary of the extensive answers received and this is in order to make it easier for the reader to follow.

When analyzing the findings in the qualitative research the authors will use both the theoretical framework as well as cross-references from the findings in the quantitative research of the companies' financial statements. This is done in order to get a broad and holistic view of the effects of IFRS 3, IAS 36 & IAS 38 on the companies' acquisition process.

The respondents of the survey held positions such as Chief Financial Officer (CFO), Head of Business Controlling and Chief Accountant. The time period, for which the respondents have had this position ranged from 5 - 13 years, which implies that they have the right knowledge and experience in order to answer the survey.

4.3.1 Goodwill

All companies but one in the study have been acquiring other businesses during the last five years. The average number of companies acquired during this period was nine. Since goodwill arises through acquisitions, this implies that most companies in the study have goodwill.

Before the new accounting standards the most common way to handle goodwill was to amortize it linear over 5 – 20 years. Three companies used an amortization period of 5 years, while the rest used 20 years. One company in the study had an individual determined amortization plan for each acquisition, but for larger strategic acquisition they used a 20-year period. One of the respondents had already amortizised all goodwill before the new accounting standards and thus, was not affected by the new rules.

When it comes to the issue of fluctuating results due to IFRS 3, the respondents' opinions differed. The majority of the respondents believe that there will be no apparent effect on the companies result. There are several reasons for this according to the respondents. First; the non-amortization of goodwill will be replaced by larger amortization of intangible assets. Second; even before IFRS 3 was implemented the companies could, if believed necessary, do a larger, one time, amortization of goodwill in order to adjust the book-value to the true fair value. Third; the result should not fluctuate since the respondents claim that they do not pay premiums higher than what the company can deal with during normal business cycles without writing down assets.

The respondents that believe that the result will fluctuate do so since the smooth, linear, amortization of goodwill is now prohibited and that there now, through IFRS 3, will be years with large impairment and years with no impairment, leading to fluctuation.

The respondents' answers to the question regarding whether IFRS 3 has made it more attractive to acquire other businesses is fairly clustered. Most companies state that they have other evaluation methods than accounting issues for acquisition decisions and that the accounting principles do not effect this evaluation. This since most acquisitions is of strategic magnitude and hence is evaluated in the companies' corporate framework and not on the basis of a single factor, like goodwill. Furthermore, one respondent claim that the aim of an acquisition is to generate free cash flow[13] and through that increase shareholders' wealth, and since goodwill impairment are not part of the cash flow, IFRS 3 will have no impact on acquisition decisions. Additionally, one company states that the annual impairment test still makes the company exposed to the risk of goodwill write-down regarding the acquisition. One of the respondents argues that IFRS 3 could make acquisitions more attractive. This will be the case when the goodwill entry represents a significant proportion of the premium paid in the acquisition. If, however, the goodwill entry is not of significant magnitude, there will be little impact.

4.3.2 Valuation of acquisition candidates

The acquisition process is performed in widely separate ways in the companies examined. Some companies have pre-defined models for the process but the factors included in the

[13] Free cash flow represents the cash that a company is able to generate after laying out the money required to maintain its asset base. It is a measure of financial performance calculated as operating cash flow minus capital expenditures. (Investopedia, 2006)

models vary. Common factors that most of the companies in the study look upon in the acquisition process are synergies, strategically aspects, growth potential, cash flow analysis and historical and future earnings. Since some of these factors are hard to measure, several other factors are included in the actual acquisition models. The figures used in these standardized acquisition models are retrieved from the income statement, the balance sheet and the cash flow analysis of the target firm and include items such as EBITDA[14] and free cash flow. Beside these models, some companies primarily look on more subjective items such as customer relations, supplier relations, product technology, products, brands and patents, this in order to identify future profitable factors in the acquisition candidate.

After the implementation of IFRS 3, some of the companies have revised their acquisition model. It is especially the companies' standardized acquisition model that has been adjusted for the non-amortization of goodwill, dismissals for restructuring costs, and the fact that assets need to be valued to its fair value. Furthermore, the non-amortization of goodwill has led to that some multiples look more attractive than before. For example the Earnings per Share multiple has increased since the goodwill entry does no longer effect earnings negatively. Additionally, one company has developed an entirely new acquisition model based on the new rules in IFRS, this in order to allocate as large proportion of the acquisition premium as possible to intangible assets, which can be amortizised. The company states that by conducting a more thoroughly analysis of the intangible assets before the acquisition the goodwill entry can be minimized and hence its effect on the companies profits can also be kept to a minimum.

When it comes to valuation and pricing of the acquisition candidates the majority of the companies are using the discounted cash flow method (DCF, see section 2.2.4). Some companies use this method in combination with an analysis of other multiples such as P/E-ratios[15], Earnings per Share (EPS), Debt-to-Equity.

All respondents claim that the new accounting standards have had little impact on the valuation method used.

4.3.3 Intangible assets

In order to identify the intangible assets of an acquisition candidate the respondents claim that the process is different from time to time and that it depends on the type of acquisition. One respondent states that the company uses all available public information in combination with their own knowledge regarding markets and products in order to categorize intangible assets. Furthermore, one respondent states that the procedure of identifying intangibles is a part of the due-diligence process and that the entire company is examined thoroughly. Additionally, another respondent argues that the company uses an informal process with the reasoning over the factors that motivate paying a higher premium in an acquisition. One company claims that it divides the difference between the debt-free price of the target and the value of its equity between machines, patents, and brand etcetera. The rest is according to the respondent, by definition, goodwill. Finally, one company states that it uses specialists in the different areas to examine the possible intangible assets. Then

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[14] EBITDA = Earnings Before Interest, Tax, Depreciation and Amortization.

[15] P/E = Price-to-Earnings ratio, i.e. the market capitalization per share divided by the companies latest known earnings per share.

a comparison is made with the figures received from the specialists and the targets balance sheet in order to determine a premium to pay.

Regarding the question of whether IFRS 3 and IAS 38 has made it easier than before to identify what actually has been acquired, the companies obviously have different practice and knowledge on this issue. A few companies state that they yet have a too limited experience in order to know the impact since the rules was implemented so recently. A majority of the respondents though states that it is going to be easier to identify the values of an acquisition candidate under the new rules since more information needs to be public and since a more accurate separation of intangibles from the goodwill entry needs to be done.

All the respondents are clear with that the new accounting standards in IFRS 3, IAS 36 and IAS 38 have not created new acquisition candidates that were not candidates earlier. The accounting issues are not the decisive part when it comes to the selection of acquisition candidates.

None of the respondents are ready to pay a higher premium in acquisitions today then earlier. One respondent states that if the higher premium does not reflect the underlying profitability and can not be activated as any kind of asset, an immediately impairment loss is existing. This implies that this effect can be as negative (or more negative) than the amortization of goodwill according to the earlier rules. A higher premium due to the goodwill is therefore offset by the possibility of impairment.

4.3.4 Other aspects

In this section, the authors will present the various aspects of the new accounting standards that do not belong to any of the previous sections.

The first part deals with IFRS 3 and the fact that assets, liabilities and contingent liabilities must now be accounted for at a fair and true value. About half of the companies in the study state that this will have no impact for the company, partly because their book-value already was close to the market value. However, the other half states that it will have an important impact. The companies states primarily two reasons for this. Firstly; since the value of the assets and liabilities will fluctuate depending on market condition, the companies' results will be harder to predict and correlate more with the overall market. Second; a major problem when valuing the target firms current assets at the market value is that until the current asset is fully used, the company can incur a loss instead of the actual profit for the goods sold. Hence, the new accounting standards can give rise to results that do not corresponds to the true profitability of the firm.

The limited ability for dismissals for restructuring costs has not affected the companies significantly. However, one respondent state that the company needs to be better prepared and that the due diligence must be more extensive than before, so they at the acquisition date can decide on possible restructuring costs. Furthermore, one company claims that it can have a negative impact on the price paid in an acquisition. This is due to the fact that if the restructuring costs can not be dismissed, the entire cost has to be expensed in the income statement, resulting in a lower profit.

The second part is connected to the question of whether the new internationally harmonized accounting standards have made it easier to acquire foreign firms. Most companies in the study state that it has had little effect on their international acquisition practice. This is due to the fact that a majority of the companies are large organizations with offices around the world, and that they, due to that, already has a good understanding of the international market and knowledge on acquisition practices in other countries. However, many companies state that the new harmonized accounting standards have made it easier to do comparisons between acquisition candidates in different countries.

The third part is concerned with the evaluation of companies after an acquisition. A vast majority of the companies in the study states that the new accounting standards will have no significant impact on the evaluation process after an acquisition. The reasons for this differ slightly, but a general description is that a cash flow analysis is the most important evaluation measure and this analysis is not affected by the new accounting standards. However, there are a few respondents that claim that IFRS 3, IAS 36 & IAS 38 will make the due diligence process more rigorous and that each acquisition candidate will be examined more carefully in order to identify the true value of its assets (fixed and intangible). The fact that more work is done before an acquisition would according to the companies imply that the evaluation process after an acquisition will become easier.

4.4 Analysis of IFRS 3, IAS 36 & IAS 38's effect on companies acquisition process

Since all the sampled companies but one has been acquiring other firms during the last five years, the authors can conclude that the sample used in the study is suitable. This since the new accounting standards IFRS 3, IAS 36 & IAS 38, according to earlier studies by e.g. KPMG (2003) and Bergin (2006) effect primarily companies engaging in acquisitions.

4.4.1 Analysis of the goodwill effect

Before the implementation of IFRS 3, the companies in the study amortizised their goodwill in accordance with the legislation in ÅRL and RR 1:00. This meant that goodwill was amortizised over 5-20 years (FAR, 2005). However, since the legislation was flexible the companies most often used an amortization period of 10-20 years. The motive for amortizising the goodwill evenly was, as also stated by Stevenson & McPhee (2005), to be able to predict the impact of earnings more accurately. Since the introduction of IFRS 3, goodwill can no longer be amortizised, and this implies that companies that used amortization over a shorter period of time should be more affected than others by the new rules. This since a short amortization period implies that more goodwill is expensed each year leading to lower profits. However, the magnitude of the effects also varies depending on the size of the goodwill entry, i.e. companies with little goodwill and short amortization time would not be affected significantly. By comparing the goodwill entry in the companies' balance sheet with the amortization time recognized in the survey, the authors can conclude that the companies using a short amortization time also have a small goodwill entry and the companies with a longer amortization time have larger goodwill entries.

The issue of fluctuating results due to IFRS 3 has as previously mentioned, shown different opinions. Most companies believe that there will be little impact on the results and that these will not fluctuate. Only a few companies agree with PricewaterhouseCoopers (2004), which stated that the new accounting standards should have a large influence on the companies' results. As stated by the authors in the quantitative research, IFRS 3 has a large impact on the companies' profits (9.52 per cent) and the results might therefore fluctuate more due to the new accounting standards. The fact that the companies view on the effects of IFRS 3 on the profits does not fully correspond to the findings in the quantitative research and to the research done by PricewaterhouseCoopers (2004), imply two things.

First; since the quantitative research only shows the change of IFRS 3 from one year to another there might be a limitation in the prediction of trends. This means that the change in profit this year might not be consistent over time. Second; since the new accounting principles have only been used for a short period of time there is a possibility that the companies have a limited knowledge of the true impact of the change due to IFRS 3. Since the findings in the quantitative research displays similar results as studies by e.g. PricewaterhouseCoopers (2004), Suneson (2005) and Rognerud (2006) the authors are confident that IFRS 3 has had a great impact on the companies' profits. However, since IFRS 3 was implemented on January 1st 2005, it is still too early to draw a conclusion regarding the trend in the fluctuation of the profits.

4.4.2 Analysis of the valuation of acquisition candidates

As described earlier (section 4.3.1) a majority of the companies state that IFRS 3 does not make acquisitions more attractive. This is due to the fact that the accounting issues are just a small part of the companies acquisition model and that they use other factors when determining acquisition candidates.

Instead of accounting issues, the companies in the study look on factors such as synergies, strategic aspects and growth potential when determining on an acquisition candidate. This is in line with Morris (2000) who claims that synergies and growth potential are the most important factors to consider when acquiring other businesses. Furthermore, some companies look on subjective items such as product technology, customer relations and patents. In order to identify these items the companies examine each aspect of the target firm carefully. This is what Morris (2000) calls the due diligence. Other aspects covered by the companies due diligence process are a thoroughly analysis of financial statements which includes items such as EBITDA and free cash flow.

The companies with pre-determined acquisition models have, due to IFRS 3, IAS 36 & IAS 38, been forced to modify these models. The models have been changed due to the fact that the amortization of goodwill will no longer effect the companies' income statement and that assets needs to be valued to its fair value. Since the companies in the study has needed to modify their models, it has, as predicted by PricewaterhouseCoopers (2004) led to an increased work load for the companies in the study during the transition period.

4.4.3 Analysis of intangible assets

When it comes to recognizing intangible assets the companies differ widely in their procedures. However, one can see that every company in the survey seems to have a method of identifying intangible assets and thus separate them from the goodwill entry. By looking at the balance sheet of the sampled companies the authors have found that most companies have been fairly efficient in re-classifying their goodwill into intangible assets. Only one of the companies in the study claims that they, in accordance with PricewaterhouseCoopers (2004) use specialists to identify the intangible assets of the target company. The fact that not more companies use these specialists are a result of a more rigorous due diligence by the companies, which also is an effect anticipated by PricewaterhouseCoopers (2004).

A majority of the companies in the study agrees with Ian Wright (PricewaterhouseCoopers, 2004) who claims that the new accounting standards, that require intangible assets to be separated from goodwill if their fair value can be measured reliable, will increase the transparency of what has actually been acquired. The companies state that the reason for this is that more information needs to be public and that more items have been separated from the goodwill entry. The companies that do not share the same opinion state that they have a too limited experience of the rules in order to give a reliable answer.

All of the companies share the same idea that the new accounting standards do not inspire them to neither pay a higher premium nor to acquire companies that where not of interest before. This is logical when compared to the answers given by the companies to the question regarding the factors they look upon when deciding to acquire another firm and the research done by e.g. Morris (2000), which claims that it is other factors than purely accounting issues that are of highest interest when engaging in acquisitions.

4.4.4 Analysis of other aspects

As stated in the sections 2.3.10 and 2.3.13 assets, liabilities and contingent liabilities must now, according to IFRS 3 and IAS 38, be accounted for to its fair value. On the question of how this has affected the companies there are rather dissimilar answers. Half of the companies say that these new rules have not affected the company and the other half says that there has been a large impact. The reason for the differences in the companies' opinions on this might stem from the fact that companies possess very divergent asset-bases. A company that for example hold a large proportion of financial assets, such as stocks, will be more affected than a company that only possess stable assets, such as cash, which usually not requires impairment. Since the stock-market in 2004 and 2005 climbed to new heights (OMX, 2006), the companies holding a large amount of financial assets have therefore been more affected than others since they needed to revaluate their portfolio to its fair value. Hence, companies with assets that are highly affected by volatile market-prices will most certainly be more affected than companies holding assets with stable market-prices.

When the assets have to be accounted for to its fair value this will probably also lead to greater insights into what has been acquired and are giving the market a better view of the success of the company and its acquisitions. This since it will become easier, for both the company and people outside the company, to identify the true values of the assets and liabilities in the financial statements. This finding is in line with the statement of Ian Wright, at PricewaterhouseCoopers (2004), which states that the new accounting standard will lead to increased transparency that will give the market greater insights.

The companies claim that the new international accounting standards have had little effect on their international acquisition practices. This can be explained by the fact that most of the companies studied are multinational companies that have a long experience in foreign acquisition practices. However, the companies are stating that the new accounting principles have made it easier to do comparisons between acquisition candidates in different countries. This finding is in line with the findings by KPMG (2003) which states that the new accounting standards will lead to increased transparency and comparability which could lead to greater consolidation within and across borders.

The new accounting standards will not have a major effect on the evaluation practices after an acquisition according to the respondents. As already concluded however, there are a few respondents that claim that IFRS 3, IAS 36 & IAS 38 will make the due diligence process more rigorous and that each acquisition candidate will be examined more carefully. This is because more analysis and time efforts are needed in order to identify the true value of assets and because of the requirement of a yearly valuation of goodwill. The separation of intangibles from goodwill and the requirement of extra disclosures will also lead to an extra work-load. These findings are first in line with the general description by Morris (2002) regarding of what constitutes the due-diligence process. Second, these finding are further in line with PricewaterhouseCoopers (2004) which state that due to IFRS 3, IAS 36 and IAS 38 greater analysis is needed on the target entity's business in advance of a transaction in order to be able to identify potential intangible assets and to determine the risk of impairment changes. PricewaterhouseCoopers (2004) also asserts that the acquisition process should become more rigorous, from planning to execution and this can be connected to the due-diligence process.

Third, these empirical findings can also be connected to the findings of Jansson et al (2004) which states that the requirement of a yearly valuation of goodwill bring additional work and substantially increased demand of information for the companies.

By comparing the number of acquisitions that each company has done with the way they have handled and adjusted their acquisition process the authors have found an interesting result. The companies that are experiencing that IFRS 3, IAS 36 & IAS 38 will make the due diligence process more rigorous and time-consuming have been engaged more frequently in acquisitions than others. It also seems that these companies have been putting more effort in the adjustment of their acquisition process and more time to the transformation to IFRS 3, IAS 36 and IAS 38. Hence, the due-diligence process will most certainly be more rigorous and time-consuming the larger the acquisition is. The authors can apply this to the statement of Peter Malmqvist, which claims that the new accounting standards regarding goodwill will primarily have a significant impact on large companies who are frequently engaged in acquisitions. (Bergin, 2006)

5 Conclusion and Final Remarks

In this chapter, the authors will fulfil the purpose of the thesis by giving a final conclusion to the problem statement. The research questions will be extensively and clearly answered together with concluding clarifications. The authors will further give a presentation of the authors own reflections regarding the thesis. This is followed by critique of the method used and finally the authors will give suggestions for further studies.

The final section of this thesis will present the conclusion of the investigation. A reminder of the purpose stated in chapter 1 is suitable since this will help the reader as a guide through the following discussions.

The purpose with this thesis is to illustrate and analyze how the new internationally harmonized accounting standard, IFRS 3, IAS 36 & IAS 38 affect the financial statements of the companies listed on the Stockholm Stock Exchange and if the new rules have an impact on these firms' acquisition practice.

The conclusion gives the reader clear answers to the research questions and will demonstrate for the reader that the authors have fulfilled the purpose of the thesis.

5.1 Conclusion

The thesis' first objective was to answer the following question:

- *How have the new accounting standards IFRS 3, IAS 36 & IAS 38 regarding acquisitions affected the income statements and the balance sheets of the quoted companies?*

The most significant impact of the new accounting standards is that operating profits has increased with approximately 9.5 per cent or 12.9 billion SEK in the 30 companies studied. The main reason for the increase in profits is due to the fact that goodwill, according to IFRS 3, no longer can be amortizised. Since most companies have not found any reasons for impairment of their assets, the positive effects of the non-amortization of goodwill overshadows the negative impairment effects. This effect can also be seen in the balance sheet where the assets and owners' equity has increased with 7 billion SEK for the companies examined. Hence, the new accounting standards IFRS 3, IAS 36 & IAS 38 have had a large impact on both the income statement and the balance sheet. The research further showed that the impact of IFRS 3, IAS 36 & IAS 38 affects all industries in a similar way.

The second objective was to answer the following question:

- *What effects do the new standards have on the Swedish firms' acquisition process and how do the companies handle these changes?*

The first conclusion drawn is that companies handle the adjustment to the new accounting standards regarding acquisitions in different ways. Some companies disregard the change and continue as before, while other has modified their acquisition practice. The authors have found that the companies that have been most frequently engaged in acquisitions are also the ones that have been putting more effort in the adjustment of their acquisition process and more time to the transformation to IFRS 3, IAS 36 & IAS 38.

A factor that most companies have in common is that they have had to adjust their standardize acquisition model for the non-amortization of goodwill, dismissals for restructuring costs and the fact that assets need to be valued to its fair value. Furthermore, the fact that the companies now, according to IFRS 3, must identify and separate the intangible assets from the goodwill entry has made the due diligence process more rigorous. The acquisition process will therefore be more time-consuming and require more resources than before. However, a majority of the companies also states that the new rules will make it easier to identify the value of an acquisition candidate since more information needs to be public and through the fact that a more accurate separation of intangibles from the goodwill entry needs to be done

Another factor in common for the companies in the study is that they do not believe that the new accounting standards have had a significant impact on their acquisition process. This is due to the fact that the decision to acquire is based on other aspects than accounting standards and that these other factors, like synergies and growth potential, are independent from the accounting issues.

One of the aspects of the new, internationally harmonized, accounting standards that have influenced the companies positively is that the standards have made it easier to do comparisons between acquisition candidates in different countries.

5.2 The authors reflections

The authors find the fact that operating profits has increased with 9.54 per cent due to IFRS 3, IAS 36 & IAS 38, rather remarkable. Logically, the authors could anticipate an increase in profits due to the non-amortization of goodwill, but an increase of around 10 per cent was more than expected. Furthermore, most of the companies in the study claim that the new accounting standards will have a small impact on the company's result and that these will not fluctuate more, this since the non-amortization of goodwill is replaced by impairment. However, the authors have found that the companies' results are highly affected by the new rules and that impairment and amortization of intangible assets has not replaced amortization of goodwill to the same degree as the companies thought. This finding was surprising since the authors believed that these effects would level out each other more than the actual outcome.

The fact that the companies view does not fully correspond to the actual figures is probably due to the fact that the new accounting standards have not been in use for so long, hence, the companies' experience of its effect is still limited. Even though the authors have recognized a significant rise in operating profits it is still too early to rule out the companies view, this since it is also too early to identify a clear trend in the profits.

Since operating profits have risen with about 10 per cent, due to the new accounting standards, and the fact that investors rely heavily on these profits it is of crucial importance that investors take the accounting changes into consideration when valuing companies. This is also a necessity for companies when valuing acquisition candidates, hence the due diligence process must become more extensive to capture the true value of the target. With the boom in overall economy and the sky-rocketing stock prices in particular, the authors question if the investors has actually taken the accounting issue into account when valuating companies. If they have not, how much of the increase in the stock prices is simply due to the new accounting standards? The most likely answer is that large institutional investors have the right knowledge in order to perform a correct valuation and hence, their investment decisions are not affected by the accounting change. However, small private investors might not possess all the knowledge regarding how to interpret the financial statements after the accounting change, and thus find it difficult to recognize what is a true profit and what is just due to the new standards. Since stock prices are mainly influenced by the larger institution, the increase in stock prices is most likely a result of the prosperous overall economy and not due to the accounting change.

5.3 Critique of the method used

Although the methods used to conduct this study have been chosen with great care to eliminate biased and skewed results, the authors are aware that some shortcomings might be present and that a few clarifications are needed.

The authors' are basing a large proportion of the theoretical framework within accounting for acquisitions on surveys and publications from auditing firms. This can be seen as a shortcoming as they might not be of scientific quality. However, the authors have used publications from all four of the major auditing firms, creating a broad view of the accounting standards. Furthermore, these publications have been examined in combination with legislative texts. The authors of this thesis believe that the fact that the auditing firms have a deep knowledge and experience of these issues and therefore, in combination with the legislative texts, the publications used are considered reliable.

As mentioned before, one can argue that using a sample size of 30 companies and only sampling them from the largest lists on the Stockholm Stock Exchange might cause a biased result. This since these companies often possesses similar characteristics and therefore might be affected in the same way by e.g. new accounting standards. However, since the aim of the chosen sample was to have a large fraction of companies frequently engaged in acquisitions, the A-list and the O-list's *Attract 40* were found to best fulfill this aim. Using a random sample consisting of all the lists on the Stockholm Stock Exchange might have yielded a more confident result on how the new standards affect all quoted companies, but the findings would probably not have been as significant as the ones found in the sample used.

In the qualitative research the response rate was merely 50 per cent, which can be seen as an inadequacy of the thesis. However, as stated in section 3.7, the main goal of the qualitative research was not to get a 100 per cent response rate, but instead to receive extensive answers of high quality from the respondents. Since 15 responses were received, out of which a majority was of high quality, the authors believe the response rate to be sufficient enough to fulfill the purpose of this thesis.

The purpose of the methodological triangulation is to establish validity through confirmation of a specific event by using multiple research methods. In this thesis it is evident that the research methods do not completely consent. This is due to a number of factors. Even though the two research methods in this thesis do not match each other fully, they do complement each other well. This since the purpose of the chosen method was to get a holistic view of the accounting change and its effect on companies' acquisition process.

5.4 Suggestions for further studies

Since the new accounting standards are so recent and the experience of its effects are yet limited it would be interesting to conduct a study in the future, including a longer time-horizon where trends can be identified. This kind of study would be interesting because there is a possibility that the companies will have a different opinion of the new rules in the future when they have gained knowledge of the long-term effects on the acquisition practise. By conducting a study with a longer time-horizon it is also possible to identify whether the results of the companies actually have fluctuated more than earlier or if the non-amortization of goodwill are offset by the amortization of intangibles and impairment of assets.

Since there are studies that claim that the new accounting rules regarding acquisitions will primarily affect larger companies it would be interesting to conduct a comparison between companies on different lists on the Stockholm Stock exchange. Since this thesis brings out a study of the largest companies on the Stockholm Stock exchange, a comparison with smaller companies can be rewarding in order to compare the outcome against the results from earlier studies. Then the claims in the earlier studies can be confirmed or rejected.

Another topic for further studies would be to conduct an international comparison between countries and thus compare the effects of the new international accounting standards in different nations. An interesting issue here is if IFRS 3, IAS 36, and IAS 38 have affected the acquisition process additionally and/or if the financial statements have been affected more in some countries than others.

Further on, the authors have found another appealing aspect to look into as a further study. This aspect is to get insights of the accountants view on the new accounting standards and its implication for the acquisition practise. It would be interesting to compare the accountants view to the companies in order to identify differences in the way they perceive the transition from Swedish accounting standards to the international accounting standards.

Finally, the authors find it important and interesting to study the whole due-diligence process by itself. By doing this the authors can get a holistic illustration of the acquisition process and look into specific acquisitions in order to spot the way companies perceive acquisitions. Then the changes, due to IFRS 3, IAS 36 and IAS 38, can be identified and tracked in a more straightforward way.

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Appendix I

Survey – IAS & IFRS 3's effects on acquisitions

1. What is your position within the company?

2. How many years have you got this position?

Goodwill

3. Have your company acquired other companies within the last 5 years?

Please select any of the following by putting an X in one of right boxes.

Yes ☐

No ☐

If yes, how many?___________________

4. How was goodwill amortized before IFRS 3?

5. Do you think that the company's result will be more unpredictable and fluctuate more when goodwill is no longer a subject to amortization?

6. Has the fact that goodwill no longer can be amortized made it more attractive to acquire other companies? Why/why not?

Valuation of acquisition candidates

7. Does your company use a special model for the acquisition process? If yes, what factors are you looking at?

8. If yes on the previous question, has this model changed due to the implementation of IFRS 3?

9. Does your company have a special model for valuation of acquisitions candidates? What kind?

Intangible assets

10. How do you proceed in order to identify the intangible assets of an acquisition candidate?

11. Is it now, under the new rules in IFRS 3, easier than earlier to identify what actually has been acquired?

12. Have the new accounting rules made those companies that earlier were not acquisition candidates to become acquisition candidates now?

13. Are you today through IFRS 3, willing to pay a higher premium in an acquisition than you was before?

Other aspects

14. What kind of effect will the new rules that assets, liabilities and contingent liabilities should be accounted for to its fair value have for the company?

15. What effects will the limited ability to do dismissals for restructuring costs have for the company and its acquisitions?

16. Have it, since the implementation of the harmonized accounting rules, become easier and/or safer to acquire companies internationally?

17. Is it now possible to make a faster evaluation and conclusion of whether an acquisition is financially successful or not? (Through the effect of goodwill on the result, the impairment test, and through harmonized accounting rules) If so, how?

Appendix II

Companies in the study:

A-list companies:

Assa Abloy
Atlas Copco
Cardo
Elekta
Ericsson
Gunnebo
Handelsbanken
Hexagon
Holmen
JM
Lindex
Nordea
Ratos
Sandvik
Securitas
SCA
Scribona
Skanska
SKF
Telia Sonera
Tieto Enator
Trelleborg
Wallenstam

O-list's *Attract 40*:

Alfa Laval
Boliden
Carnegie
Eniro
Gunnebo Industrier
MTG
Rottneros

Appendix III

Company	Alfa Laval	Assa Abloy	Atlas Copco	Cardo	Hexagon	Gunnebo Ind	Sandvik	SKF	Trelleborg
Industry	Industrial	Industrial	Industrial	Industrial	Industrial	Industrial	Industrial	Industrial	Industrial
Income Statement									
Impairment								-17	
Goodwill	191,5	978	432	90	99	-0,8	354	70	403
Negative Goodwill								-1	
Amortization of Intangibles								-117	-24
Result of IFRS Adj	**191,5**	**978**	**432**	**90**	**99**	**-0,8**	**354**	**-65**	**379**
Operating Profit	**1438,4**	**3683**	**6651**	**-1**	**686**	**126,4**	**7578**	**4434**	**1891**
IFRS Adj / Operating Profit	**-6,9%**	**26,6%**	**6,5%**	**-9000,0%**	**14,4%**	**-0,6%**	**4,7%**	**-1,5%**	**20,0%**
Balance Sheet									
Goodwill	191,5	-95		90	50	-9		128	403
Negative Goodwill								8	
Intangible Assets		79	360		16	15	341	47	
Dismissals for Restructuring costs									-24
Impairment								8	
Total	**191,5**	**-16**	**360**	**90**	**66**	**6**	**341**	**191**	**379**

Total IFRS Adjustment	**2457,7**	**273,08**
Total Operating Profit	**26486,8**	**2942,98**
Total IFRS Adj / Total Operating Profit	**9,28%**	
Euro	**9,13**	

Company	JM	Skanska	Wallenstam
Industry	Construction/Real Estate	Construction/Real Estate	Construction/Real Estate
Income Statement			
Impairment		-45	
Goodwill	13	405	59,9
Negative Goodwill			
Amortization of Intangibles			
Result of IFRS Adj	**13**	**360**	**59,9**
Operating Profit	**792**	**4361**	**1818**
IFRS Adj / Operating Profit	**1,6%**	**8,3%**	**3,3%**
Balance Sheet			
Goodwill	13	334	
Negative Goodwill			
Intangible Assets		24	4,8
Dismissals for Restructuring costs			
Impairment			
Total	**13**	**358**	**4,8**
Total IFRS Adjustment	**432,9**	**144,3**	
Total Operating Profit	**6971**	**2323,7**	
Total IFRS Adj / Total Operating Profit	**6,21%**		

Company	Boliden	Holmen	Rottneros	SCA
Industry	Mining	Pulp&Timber	Pulp&Timber	Pulp & Consumer goods
Income Statement				
Impairment				
Goodwill	165			1233
Negative Goodwill				
Amortization of Intangibles		32		
Result of IFRS Adj	**165**	**32**	**0**	**1233**
Operating Profit	**1831**	**1860**	**-114**	**7669**
IFRS Adj / Operating Profit	**9,0%**	**1,7%**	**0,0%**	**16,1%**
Balance Sheet				
Goodwill	165	32		1161
Negative Goodwill				
Intangible Assets				28
Dismissals for Restructuring costs				
Impairment				
Total	**165**	**32**	**0**	**1189**
Total IFRS Adjustment	**1430**	**358**		
Total Operating Profit	**11246**	**2812**		
Total IFRS Adj / Total Operating Profit	**12,72%**			

Company	**Eniro**	**Ericsson**	**Scribona**	**Telia Sonera**	**Tieto Enator**
Industry		Telecom	IT&Communication	Telecom	IT-consulting
Income Statement					
Impairment					-170,731
Goodwill	347	476	8	1645	534,105
Negative Goodwill					2,739
Amortization of Intangibles					-28,303
Result of IFRS Adj	**347**	**476**	**8**	**4730**	**337,81**
Operating Profit	**1232**	**26706**	**98**	**18793**	**1485,451**
IFRS Adj / Operating Profit	**28,2%**	**1,8%**	**8,2%**	**25,2%**	**22,7%**
Balance Sheet					
Goodwill	288	442	8		
Negative Goodwill					
Intangible Assets	55				-28,303
Dismissals for Restructuring costs					
Impairment					
Total	**343**	**442**	**8**	**0**	**-28,303**
Total IFRS Adjustment	**5898,81**	**1179,76**			
Total Operating Profit	**48314,45**	**9662,89**			
Total IFRS Adj / Total Operating Profit	**12,21%**				

Company	Carnegie	Handelsbanken	Nordea	Ratos
Industry	Bank/Investment	Bank/Investment	Bank/Investment	Bank/Investment
Income Statement				
Impairment				
Goodwill	5	269	1469,93	65
Negative Goodwill				
Amortization of Intangibles				
Result of IFRS Adj	**5**	**269**	**1469,93**	**65**
Operating Profit	**554**	**13056**	**20852,92**	**2155**
IFRS Adj / Operating Profit	**0,9%**	**2,1%**	**7,0%**	**3,0%**
Balance Sheet				
Goodwill	5	475	1469,93	
Negative Goodwill				
Intangible Assets		-11		65
Dismissals for Restructuring costs				
Impairment			-264,77	
Total	**5**	**464**	**1205,16**	**65**
Total IFRS Adjustment	**1808,93**	**904,465**		
Total Operating Profit	**36617,92**	**18308,96**		
Total IFRS Adj / Total Operating Profit	**4,94%**			

Company	**Gunnebo**	**Securitas**
Industry	Security	Security
Income Statement		
Impairment		-100
Goodwill	75,1	1150
Negative Goodwill		
Amortization of Intangibles	-94,8	-26
Result of IFRS Adj	**-19,7**	**1024**
Operating Profit	**284**	**3900**
IFRS Adj / Operating Profit	**-6,9%**	**26,3%**
Balance Sheet		
Goodwill	75,1	794
Negative Goodwill		
Intangible Assets		433
Dismissals for Restructuring costs	-94,8	
Impairment		
Total	**-19,7**	**1227**
Total IFRS Adjustment	**1004,3**	**502,15**
Total Operating Profit	**4184**	**2092**
Total IFRS Adj / Total Operating Profit	**24,00%**	

Company	Elekta	Lindex	MTG
Industry	Healtcare	Consumer go	Media
Income Statement			
Impairment			
Goodwill		27,76	91
Negative Goodwill			
Amortization of Intangibles			
Result of IFRS Adj	**0**	**27,76**	**91**
Operating Profit	**364**	**390,7**	**1057**
IFRS Adj / Operating Profit	**0,0%**	**7,1%**	**8,6%**
Balance Sheet			
Goodwill		27,76	91
Negative Goodwill			
Intangible Assets	25		-30
Dismissals for Restructuring costs			
Impairment			
Total	**25**	**27,76**	**61**
Total IFRS Adjustment	**118,76**		**59,38**
Total Operating Profit	**1811,7**		**905,85**
Total IFRS Adj / Total Operating Profit	**6,56%**		