E-business acquisition under IFRS 3 - An analysis on a revised standard

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**Summary**

In this study we have analysed if the revised IFRS 3 has changed the accounting procedure of e-business acquisitions, in other words when an e-business (online business) acquires another e-business. We have chosen to conduct the study with CDON Group AB as a reference company. The study is primarily using a mixed research method, in other words a mix of quantitative and a qualitative method. The data analysis applies the philosophy of positivism. In this thesis we have assumed the entity theory to be true, and this theory is a suitable accounting theory, which views the company itself as the responsible one for its liabilities and assets. The assumption that the entity is a separate person enables us to view the company apart from its owners and thereby assume that the management of assets, and the acquisitions are an act of CDON Group’s best interest. We have analysed the official financial statement of CDON Group AB from the years 2007-2013, but also the financial statements from each of the four acquired companies, NLY Scandinavia AB, Gymgrossisten Nordic AB, Rum21 AB and Tretti AB. Findings show key differences in the revised IFRS 3 when compared to its previous versions. Main differences are the transaction cost that should be included in the consideration, furthermore, how to divide the consideration when including an additional acquisition. The study discusses that the revision of the IFRS 3 might only affect the reporting procedure of an acquisition, the underlying figures are still there, however, the underlying figures might have been included in another entry and/or changed part in the statement. Thereby the study is identifying a change in the reporting procedure of acquisitions after the revised IFRS 3.
Preface

With this bachelor thesis our first three years in the International Business Program at Umeå University has come to an end. We would like to thank the people around us who have shown an appreciation and been supportive during this time. Furthermore, we would like to thank Tina Romanov, Niklas Howell and Fredrik Näslund who has helped us to proofread our thesis.

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1. Introduction

In the following thesis we will discuss, analyse and interpret company acquisitions made by the largest Swedish online business. This includes how the implementation of the revised IFRS 3 has affected the use of acquisition method, and how the consideration, intangibles and goodwill has been booked and accounted for. We will start with an introduction to our subject and the problem background we identified. In the analysis the thesis will study the acquisitions before and after the implementation of the revised IFRS 3 in an e-business with a focus on the reporting changes, when a change in the standards occur.

1.1 Subject

The thesis is focusing on how a revision of a standard can affect an accounting procedure in a listed e-business. To investigate this issue the authors have analysed acquisitions and how the acquisition methods in IFRS 3 have affected the accounting procedure, also the approach taken during acquisitions (FAR Akademi, 2013, p. 130). Specifically, we will look at the “new”, rapidly expanding, emerging online retailing market, which is usually included in the well known concept of e-commerce (Turban et al., 2012, p. 4).

Previous research shows that there are many different valuation techniques and theories in use today, within the area of company acquisitions, including discounted cash-flow, avoid cost model, relief from royalty and the equity theories (Olsen & Halliwell, 2007, pp. 67-70; Riahi Belkaoui, 1992, pp. 233-236). Since the e-market is a growing market, we found it very interesting to study an expanding business and how the company develop its accounting procedure as it is expanding. We have analysed some previous literature within the subject of e-market, and narrowed it down to find a doable subject. An interesting question that arose, was how the standard that regulates business combinations, the revised IFRS 3 has affected the use of acquisition method and accounting procedure. To help us analyse the question, we are going to assume that the equity theory of entity is true.

The entity theory is based on assumption that the company itself is the owner of its assets and liable for its liabilities (Schroeder et al., 2001, p. 444). The positivism states that the collection of data should reflect the reality (Saunders et al., 2012, p. 134).

The entity theories can help in the sense that if we see that the use of assets are used in the company's best interest, the theory is putting the company at centre and this will make the income a matter for the company and not a direct contribution to the owners.
1.3 Problem background

1.3.1 Internet in Sweden

In this paper we will concentrate on the Swedish e-commerce market and in particular the expansion through acquisitions of one chosen company.

The fact that Sweden is one of the top users in the e-market (E-Barometern, 2013, p. 6), makes us believe that the Swedish market is a very suitable market to do research within this subject. The annual report of E-Barometern shows that the e-market has grown and spread rapidly in Sweden the last ten years, the market in monetary terms has increased by nearly eight times since 2003 (E-Barometern, 2013, p. 7). One of the reasons for that, is that Swedish people are among the most internet connected people in the world (E-Barometern, 2013, p. 6). We argue that an analysis of the change in reporting procedures during acquisitions conducted by Sweden's largest e-business, CDON Group AB, will result in a realistic tendency of how an e-business acquires another e-business.

1.3.2 International Financial Reporting Standard

When the International Financial Reporting Standards (IFRS) became mandatory for all Sweden's publicly traded companies in 2005 (Hamberg et al., 2011, p. 266), one of the major changes from the older rules of accountancy in Sweden was the IFRS 3. That major change had a lot to do with the change from amortisation of goodwill. The new standard regulate that goodwill should be impaired by a yearly recognition to a fair value (Hamberg et al., 2011, p. 266). It also requires new procedures in the identifying process of intangibles and for the identification of goodwill. In the older international standard, the IAS 22, this was not necessary, since the difference between the acquired firm's book value and the consideration was seen as goodwill (Hamberg et al., 2011, p. 266). One of the consequences of implementing the IFRS 3, was that the impairment of goodwill became lower than the amortisation level had been in the older standard (IAS 22) (Hamberg et al., 2011, p. 264). The standard states that this first contribution of IFRS 3 was in use until the revised IFRS 3 was implemented in July 1, 2009 (FAR Akademi, 2013, p. 141)

CDON Group AB has applied the revised IFRS 3 from January 1, 2010. As a result, this study concentrate on differences between accounting procedure and acquisitions made under the “old” IFRS 3 and the revised IFRS 3 (CDON Group AB, 2012, p. 56). To do that we will study acquisitions before January 1, 2010, namely NLY Scandinavia AB and Gymgrossisten Nordic AB. After January 1, 2010, we will analyse the acquisition of Tretti AB and Rum21 AB.

Another main difference in the revised IFRS 3 is what is included in the consideration. For example, transaction costs are seen as expenses instead of being seen as a part of the consideration under the revised IFRS 3 (PWC, 2008, pp.8-9). This change in the standard can thereby affect the earnings, as the expense is booked directly in the income statement. Furthermore, earn-outs (contingent consideration) do not need to be
probable, meaning that it is not obliged to occur. Also the previous held interests in the acquired business must be a part of the consideration after calculated to a fair value. This is conducted when the interest is becoming a majority interest (PWC, 2008, pp. 8-9). Further on, the revised standard gives an option to recognise "full" or "partial" goodwill when acquiring less than 100 per cent of the company at one time (Lönnqvist, 2012, pp. 94-95). To our study one major difference that we will look at, is the changes in what is included in the consideration and how that has affected the accounting procedure on the acquired company.

1.3.3 Company background

The parent company CDON is a virtual (pure play) company, that conducts business solely online (Turban et al., 2012, p. 5). The CDON Group consists of ten online stores, operating in four different business areas and in five different countries:

- **Entertainment** - Cdon.com, Lekmer.com and Bokplus.fi
- **Fashion** - Nelly.com, NLYman.com, HEPPO.com and Members.com
- **Sports & Health** - Gymgrossisten.com (fitnessstukku.fi), Bodystore.com and Milebreaker.com
- **Home & Garden** - Tretti.se and Rum21.se

(CDON Group AB, 2014a)

CDON Group AB has by acquisitions of companies, creation of new ones and invasion into new segments expanded their turnover. For example, CDON Group AB expansion has increased in average by 36 per cent annually from the years 2007 to 2009 (CDON Group AB, 2012, p. 1). From the introduction on the Swedish stock market in the late 2010, CDON Group AB increased their sales by over 100 per cent to the end of 2012 (CDON Group AB, 2012, p. 1). During this time the parent company has acquired eight companies and thereby not only entered new markets but also updated their logistics by acquiring a logistic company (CDON Group AB, 2012, pp. 7-11). Before 2010 CDON Group AB was named MTG Internet retailing AB.

1.4 Problem statement

By analysing the subject of e-commerce, and the companies closer, the issue of how the valuation of an intangible business would be conducted in a reliable way appeared. In other words, an acquisition of a pure electronic platform, with just a small warehouse and a few employees who is expanding. Is the solution just to value the intangibles and tangibles to their fair value according to IAS 38, IAS 16 and IFRS 3 (FAR Akademi, 2013, p. 663; p. 417; p. 130), or are the mother company paying a premium resulting in a large goodwill? This arguments and questions lead to the question of how the accounting procedure has changed in a rapidly expanding business, and if it is visible through the official financial statements. Previous literature has not focused on how a revision of a standard can effect a growing industry, as in this case an e-business and its expansion. Is the accounting procedure affected in a negative manner, that can result in a change in earnings, or is the accounting procedure unchanged?
From a research conducted about Finnish auditors in 2013 the authors came to the conclusion that there is room for subjective judgement in valuing intangible assets, such as, goodwill (Pajunen & Saastamoinen, 2013, p. 258). Findings of this study made us even more eager to see how the revision of IFRS 3 has affected acquisition methods and the change of reporting among e-businesses.

We combined the issues mentioned and discovered a gap in previous research, the gap lead us to the development of a problem statement that will contribute to fill the gap. We will investigate and analyse the issue by answering the question:

**Research Question:** Has the implementation of the revised IFRS 3 changed the reporting procedures in how a listed e-business acquires another e-business?

**1.5 Purpose**

We want to investigate how the implementation of IFRS 3 has changed the reporting procedure during the acquisition when an e-business acquire another e-business, to see if there is a difference before and after the implementation of revised IFRS 3. The research analyses an expanding e-business through acquisitions, to increase the knowledge of how the group deal with excess value and goodwill in the purchase of a more or less intangible business, also how the additional acquisition (that is, both contingent consideration and deferred acquisition) are handled.

**1.6 Contribution**

Contribution of this study is to increase the knowledge of how a revision in the standard, can change an accounting procedure for listed companies, who have plans of making a purchase of an online business. Research findings in this thesis might help management to see different valuation techniques, and help them get a better overview of the acquisitions, and how it is booked. Furthermore, we want to help future accounting students to understand the acquisition procedure of an online store and with this information they might receive an understanding that can help them to compare the accounting procedure with a non internet-based business as well. An example of a comparison could be the subjectivity that is used when valuing an intangible asset and how the consideration can be changed when the applied accounting standard is revised.
1.7 Limitations

To be able to conduct a research on the change of a reporting procedure, acquisitions and how the largest e-business in Sweden has handled the expansion through acquisitions and mergers, we had to limit our research. This in order to receive a reliable result. A limitation of this study can be the fact that we have chosen a mixed method research and analysed archival data. An additional qualitative study could use interview data to complete our secondary archival data. However to do a qualitative reliable study, we would have to conduct a combined study with interviews and archival analysis, which would demand more time than it would contribute in the framework of a bachelor thesis. The use of a quantitative method would have demanded more statistical data that can be compared to draw conclusions in a reliable manner.

Our study is based on archival analysis and this will contribute with enough reliable data to analyse and implement an answer to our research question. However, further examination of how managers think when evaluating merger and acquisitions of e-businesses can use other research methods such as qualitative case study with interviews as a way of extending the generalisation of research findings to other organisational settings. However, we think that conducting an interview will not contribute enough to our study since we are conducting a study on historical and accessible data and we will investigate one company and its acquisitions. Since this study is aiming to explain a change of reporting that is limited by standards we are confident in our data and aware of the mentioned limitations. On that basis, we think that an archival study is more preferable due to the possibility of influenced interviews, and the fact that we want numerical data which is done according to standards, without too much subjectivity. From our data collection we have received enough data to be able to do a reliable analysis of the chosen subject.

Another limitation is that we had to limit our research to only include the years of 2007 to 2013, this will not cover every merger or acquisition the company has experienced. However, we believe these years will cover the major acquisitions, since the parent company was established in 2007 when they bought their first affiliate, Nelly.com. The parent company became introduced on the Swedish stock market in December 14, 2010 under the new name CDON Group AB (previously MTG Internet Retailing AB)(CDON Group AB, 2009, p. 1). We thereby finds it interesting to limit our research on these years both before and after the introduction, the implementation of the revised standard and at the beginning of the expansion.
1.8 Disposition

Chapter 1 - Introduction

This chapter starts by introducing the topic of this thesis. We explain how we ended up with this topic before finding key concepts. Problem background and problem statement follow. Explanation of the purpose of our thesis and potential limitations conclude the chapter.

Chapter 2 - Methodology and Philosophy

In the second chapter we start by describing our chosen philosophy and explanations of the main philosophies. This is followed by the chosen approach and strategy. Further on we discuss method for data collection and the data. The chapter ends with a discussion of reliability and validity of the method applied in this study.

Chapter 3 - Theoretical Framework

Starts with a discussion of the relevant theories and describes the theories we have chosen to use in our study. The theory is followed by a review of the relevant literature in the field.

Chapter 4 - Results

In this chapter we will communicate our results in a rather straight forward line. The results are backed up by copies of the official acquisition analysis tables to make it easy for the reader to follow our argument. We start by describing the acquisition of NLY Scandinavia AB, followed by Gymgrossisten Nordic AB that took place before the implementation of the revised IFRS 3. In the next part of the chapter we discuss the acquisitions of Rum21 AB and Tretti AB.

Chapter 5 - Analysis

In this chapter we, first explain in detail the different acquisitions. We follow the same order as in the result chapter. Detailed analysis is followed by a main concluding analysis section in which we discuss different aspects of implementing IFRS 3 and the underlying valuation techniques that can have affected the acquisition.

Chapter 6 - Conclusion

In the last chapter we will have a general discussion of how the work has proceeded and our final standpoint on concluding results, interpretations and contributions.
Chapter 7 - Recommendations to further research

In this short chapter we will discuss our recommendations to further research within this subject.

Chapter 8 - Ethical issues

In this chapter we discusses briefly the ethical issues we had in mind when conducting this study.

Chapter 9 - Acknowledgement

Acknowledgements on how the work was divided and how it has proceed, we end this chapter with information of the most recent divestment.

Chapter 10 - Reference List

A list of our used references published in alphabetic order.

1.8 Definitions

**E-commerce**: “The process of buying, selling, or exchanging products, services, or information via computer.” (Turban et al., 2012, p. 4).

**E-business**: A business that is mainly engaged in the electronic market. This definition is wider than the term e-commerce, and further includes more electronic elements in their day-to-day business (Turban et al., 2012, p. 4).

**E-market**: Or Electronic marketplace, is an online meeting place where buyers and sellers conduct their businesses (Turban et al., 2012, p. 5).

**IFRS 3**: International Financial Reporting Standard act number 3, is about business combinations and the acquisition method. IFRS 3 provides that the assets and liabilities should be valued to fair values on the specific day of acquisition (FAR Akademi, 2013, p. 130).

**IASB**: International Accounting Standards Board, an organisation responsible for setting the International Financial Reporting Standards (IFRS, 2013)

**IAS**: International Accounting Standards, an older accounting standard used for large companies in Europe and those noted on the Swedish stock markets (FAR Akademi, 2013, pp. 329-770). Still used in the United States.

**Goodwill**: An intangible asset that arises with an acquisition on premium value due to valuation of example a strong brand, good customer relation or high intellectual capital. (Lönnqvist, 2012, pp. 37-45)
Virtual (Pure-play) organisations (online businesses): An organisation that only conduct their businesses online (Turban et al., 2012, p. 5).

URL: Is a short for “Uniform Resource Locator”, in other words “Internet addresses” (Turban et al., 2012, p. 424).

Additional Acquisitions: Part of consideration that is paid either as a contingent consideration or as a deferred acquisition (CDON Group AB, 2012, p. 65).

Contingent consideration (Earn-outs/optional acquisition): A part of the consideration that is disconnected to the whole sum and is dependent on future performance, it can be both positive and negative and in different mean of payments (PriceWaterhouseCoopers [PWC], 2008, pp. 9-10).

Deferred Acquisition: A part of the consideration that is deferred and is thereby paid later than the acquisition date (CDON Group AB, 2012, p. 65).
2. Methodology

In this chapter we will explain which methodological approach we have used to collect and analyse the data to conduct our research. Furthermore, we will discuss the reliability and validity of this study.

2.1 Philosophy

The four main philosophies that are discussed in business research are, the positivism, the realism, the interpretivism and the pragmatism, these wide philosophies fits in different studies and is combined in many ways (Saunders et al., 2012, p. 140).

Interpretivism concerns the difference in people as social actors, the research is usually conducted among individuals rather than about objects (Saunders et al., 2012, p. 137). A second philosophy is the pragmatism, which can be seen as combining multiple philosophical positions to find the most appropriate one, with a strong focus on the research question (Saunders et al., 2012, pp. 129-130). The philosophy of what considers as acceptable knowledge is known as the epistemology and one branch of the epistemology is the realism (Saunders et al., 2009, p. 114). The philosophy of realism, which views the epistemology in the sense of that the reality exists disregarding of our knowledge of it, what we experience is independent of our mind (Saunders et al., 2012, p. 136). The realism can be sorted into two areas, direct and critical realism, where direct realism views the objects as they are and critical realism see the objects as images of what they are (Saunders et al., 2012, p. 136). Moreover there is positivism, which can be seen as a philosophy that is familiar in studies of natural sciences, the view states that as a researcher you will prefer to collect data that is an observed reality, for example historical data (Saunders et al., 2012, p. 134). The only phenomena that can be considered "reality", is the one that we can observe with our senses (Bryman, 2005, p. 27). During the analysis the researcher then search for regular patterns in the data, and from that creating generalisations (Saunders et al., 2012, p. 134). An important factor of the positivist stance, is that the research has to be value-free as far as it is possible (Saunders et al., 2012, p. 134).

We have chosen to use a positivistic philosophical standpoint in this study, since we are collecting our data from existing financial statements, which, in our case will be the observed reality (Saunders et al., 2012, p. 134). With the assumption of the entity theory to hold, that is, the company act for its own good, we can then see the financial statements as true and is reflecting the reality, this in turn, supports the standpoint of positivism in the sense that positivism is collecting data that is historical and cannot be altered neither by us nor other users of the statements (Saunders et al., 2012, p. 134).
To see the nature of the reality and how the world operates is explained by the ontology. The two aspects of ontology is objectivism, where you see the entity or events as independent, and the subjectivism as dependent of the presence of social actors (Saunders et al., 2012, pp. 130-131). The assumption that the entity theory holds, is suitable when a research has an objectivistic view of the ontology, as in this thesis. This assumption of theory will be combined with the philosophical view of positivism which gives the thesis a stronger philosophical standpoint as the research is based on historical data.

As researchers we are neutral in our results, analysis and outcome, this further strengthen our choice of positivism (Saunders et al., 2012, p. 134). Furthermore, CDON Group AB is the leading, and the largest e-company in Sweden, it is plausible to believe that our conclusions can be seen as a general tendency for the Swedish e-market as a whole. Since we are analysing international standards, which almost can be considered as laws, we believe that we will be able to generalise our results.

Another important aspect of the study, is the multi-level of the subject, we must keep in mind that the business, and we as researchers, are on different levels and have different views of the world (Saunders et al., 2009, p. 115). To apply this on our study, we refer to Pajunen & Saastamoinen (2013) where the authors state that the managers can manipulate the numbers to maximise the earnings. Also, though the official financial statements are conducted according to established standards, the view we receive from the outside can be pure images of the underlying financial decisions.

### 2.2 Data Collection

The data were collected from the official financial statement of CDON Group AB and its subsidiaries between the years 2007 to 2013. We have retrieved the financial statements mainly from CDON Group AB's own webpage. However, to retrieve the statements of 2007 and 2008 we were forced to use a database called "Retriever Business" accessed through Umeå University library. We also used Retriever Business to collect the subsidiaries official financial statements.

The study retrieved secondary data from the companies official financial statements, the data contain mostly numerical data and can be obtained from tables and text within the statements. We found most of our relevant data in the notes of the *acquisition analysis* on the official financial statements. By analysing the years of importance, we searched for changes and how the acquisitions had emerged, as well as how the additional acquisitions was dealt with. The collection technique is done with an objective critical mindset due to the mentioned risk of some subjectivity. However, we have absolutely no reason to believe that this can be the case, but we must see the figures as a third party, in other words, as outsiders from of the companies involved.
The acquirer is MTG Internet Retailing AB, who have changed name to CDON Group AB in 2007. Furthermore, MTG Internet Retailing AB has with the name change also changed their organisational structure. We found a more appropriate summary of the acquisitions made between 2007 to 2009 in the official financial statement from CDON Group AB 2009. Therefore, we have not analysed the official financial statement by MTG Internet retailing AB from 2007 and 2008. Instead, this study uses the summary found in CDON Group’s 2009 official financial statement, and the subsidiaries own official financial statement from those years.

We have applied a data collection method that is a simple mixed method research, in other words a mix between the quantitative and qualitative, the reason for applying the mixed method is the study’s analyse of secondary numerical data as well as cases and reports (Saunders et al., 2012, pp. 165-166). The reason for rejecting a pure qualitative method is, as we have stated above, that it would demand more time that the study has to its disposal and the lack of in-dept data.

The data from the official financial statements of the analysed companies can be read by others and is unchangeable. Therefore we believe that the use of a mixed data collection method in this thesis will contribute to a more reliable result. Furthermore we have chosen the method primarily because it fitted our philosophical view as well as our study with a positivistic mindset and the data available.

The quantitative as well as the qualitative method can be seen as methods of collecting data, summarise, analyse and draw a conclusion of the analysed data, but in different procedures (Saunders et al., 2009, p. 151). The quantitative method is primarily used when conducting an experimental research, a survey research or a descriptive study. It can be a favourable method when the research project is large and when there is a large sample (Saunders et al., 2012, p. 163). Whilst the qualitative method is more appropriate to use in, for example, a case study (Saunders et al., 2012, p. 163). The qualitative method consists of a more in depth analysis and is often used in combination with interviews, the method is preferable when the data is non-numerical and more of an intangible nature (Saunders et al., 2009, p. 151).
2.3 Approach

There are three main research approaches *Deductive, Inductive* and *Abductive* (Saunders et al., 2012, pp. 143-148).

The deductive approach can be explained by the following steps: First, start by a search for an explanation of unexpected links between variables. Second the procedure demands a thorough search in literature, which results in the third step, finding hypothesis from that literature. To test and/or analyse the hypothesis found, the fourth step is the collection of quantitative or qualitative data in an unbiased manner. Fifth, the data is tested or analysed and is resulting in a drawn conclusion (Saunders et al., 2012, pp. 145-146).

A second option would be to do an inductive approach, that means that we would have to create a theory (Saunders et al., 2012, p. 146). The process of conducting an inductive approach is done in the following procedure, it usually start with collection of qualitative data, for example interviews to earn a sensation of the identified issue. Further on, the researcher needs to analyse the issue and develop a theory on the identified issue (Saunders et al., 2012, p. 146). If the study would apply the inductive approach, it would have collected our data from the official financial statement. After the analysis of the official financial statements from the different cases, the study would have to build a theory that would be applicable to all the included cases. This approach is therefore not appropriate to use in this research since this thesis is investigating historical data and draws conclusions from an existing theory. Nevertheless it could be an important approach to use in a similar but larger research, therefore it is important to mention and to have in mind.

The third and last option is the Abductive approach, which means that the research needs two different approaches. In other words, it is a mix of the deductive and the inductive approach, which means that the abduction is not building theories, but it is not testing theories either, it rather goes from theories to data and back to theories (Saunders et al., 2012, p. 147). One way to get an understanding is to think of abduction as a method of exploring a phenomenon and drawing conclusions to explain that phenomenon (inductive). To complete the abductive method you need to use your drawn conclusions from the previous phenomena and use them on new data (deductive), this will contribute to earn knowledge of how the phenomenon can contribute to your research (Saunders et al., 2012, pp. 147-148). This study could use this approach in the framework of a field study with both qualitative and quantitative methods. The study could then build a theory of the e-business market and later test the theory on a different market. This would demand a greater amount of time and resources, and it would not be convenient in a bachelor thesis.

The most appropriate approach for this thesis, regarding to our data and the research conducted, is the deductive approach. The arguments for this choice of approach is strengthen with the fact that we will not create a theory, we will rather assume that the entity theory holds, and use this facts combined as a guidance for analysing the
acquisitions. The research will use hypothesis to aid us in answering the research question, which strengthen the fact that the research are going to use a deductive approach.

To continue our research, we move on to the study we have chosen. Saunders et al. (2009) mentioning three different types of studies, Exploratory, Descriptive and Explanatory. The exploratory, is a study where the researcher wants to find out what is happening. That would not fit our research, since we do already know what is happening, and that is an acquisition of a company. The descriptive study, is usually a study conducted after an exploratory, and is describing what is happening. With this type of study we would not be able to answer our research question, and therefore we have avoided it. The last study, the explanatory study, is focusing on explaining what is happening, in other words explain relationships between variables within the research. This study would fit our research and help us answer our research question since we are focusing on explaining a relationship between variables before and after a change in the reporting standards.

2.4 Strategy

The Strategy we have adopted is close connected with the strategy of data collection but is important to state. This study applies the archival analysis, which means that we have used records and documents as primarily resources (Saunders et al., 2009, p. 150). In our case, the documents and records are official financial statements of the CDON Group AB and its subsidiaries, which we will analyse in both figures and text. This will lead to conclusions about the procedural changes that occur due to the revision in the International Financial Reporting Standards.

2.5 Reliability and Validity

This thesis is reliable due to that we have interpreted the numbers, the text and the notes in the official financial statement as they are written and the value as it is stated. Because we have assumed the entity theory to hold, we therefore have assumed that the text, numbers and notes therein are for the company's best interest and therefore are correct. The figures in the official statements are in compliance with international accounting standard. Thereby it is not biased in a way that force us to revise the data in any other way. However, we do not know how the valuation itself has been made, and thereby we cannot calculate if the premiums are too high, or in order with their policy and the purchase negotiation process.

Thereby the study is confident that if someone else would do the same research, during the same sample years, they would find the same answers as in this study when interpreting the same figures. This will enhance the reliability (Saunders et al., 2012, p. 192).
Moving on to the validity of our research. In other words, do our research concern what we want it to concern? (Saunders et al., 2009, p. 157). Factors that will affect the validity can be discussed. Factors that could affect the validity could be that we were not able to analyse every single word written in the notes. Furthermore, we do not have access to internal information such as meeting minutes from valuation and negotiation meetings. As it is now, without interviews, we can only rely on the hard fact we can collect from their own webpage, and proceed from there. However, since we are conducting a mixed method research, we are going to analyse the hard fact and other relevant information given, to gain an understanding of how the revised IFRS 3 has changed the reporting procedure.

We believe that to have a perfect validity in our study it is not enough to conduct interviews within the management of CDON Group, AB we believe that the interviewer would need to have some influence to get a straight answer. As stated earlier, most of the questions concerning the valuation of a future acquisition is classified information, regardless if it is before or after the change of the IFRS 3. We believe that the lack of interviews is acceptable and would not affect the validity. We argue that we have a valid and reliable research.

The philosophical approach of positivism allows us to generalise our conclusion to the whole market, but since we only conduct an analysis of the largest e-company in Sweden, we might not be able to generalise to the whole market, but we might be able to generalise our conclusions to the Swedish e-market.
2.6 Search strategy

The articles mentioned and described within the study, are collected from Umeå University library's database as well as a database called Google Scholar. The study has focused the search for articles to a few specific keywords, including, *valuation, goodwill, IFRS 3* and *e-commerce*. The complete list of keywords, that have been used in the study, can be found in the appendix. The reason for using these keywords, were to try and find some relevant information within the subject of e-commerce, but also to expand the study's information about accounting procedures. The strategy to find relevant articles and information were to search for keywords, then read and analyse the different articles, to mainly find relevant articles to use, but also to find a gap in the information where this study could contribute.

In this study the authors has used sources from books, articles, webpages and official financial reports, this wide collection is enhancing the reliability as well as the validity of the thesis. One can discuss the age of some of the books we are using, such as Kam V. (1990) and Riahi Belkaoui, A (1992). However, those sources are well cited and also written by authors with great knowledge in the specific areas. Therefore the literature is carefully selected after a thorough analysis. This thesis has used a lot of data from CDON Group AB directly, this in form of press releases and financial statements. The reason for not using other sources is that most of the relevant articles is based on the information given from the official press releases and financial statements. Other sources on the same data is therefore less reliable since it is a secondary source.
3. Theoretical Framework

The chapter is structured in two main parts, where we in the first part will discuss suitable theories that we can apply in this research. The second part will have a thorough analysis of different literature regarding the chosen subject.

3.1 Theory

To find an appropriate theory that can be connected to our study we have, in the review analysed a number of earlier research papers to earn knowledge of how the area has been studied and where the gap is. We have found some relevant theories of equity which is suitable for this study. The main theories are the **Entity theory**, **Proprietary theory**, **Fund theory** and also the **Agency theory**. These theories will be described to earn a knowledge in how the firm can operates as a separated part from the owners in different settings, furthermore how an agency relationship can look like.

3.1.1 Entity Theory

The entity theory analyses a business organisation as a separate unit distinct from the owners (Riahi Belkaoui, 1992, p. 234). This theory sees the entity as the owner of its resources and thereby also liable towards its owners and creditors, this leads to the view that the equity holders is both stockholders and creditors (Schroeder et al., 2001, p. 444). To get an easier understanding on the previous sentence, we can see that this leads to one of the most important equations in accounting and the basics of the balance sheet: 

\[ \text{Assets} = \text{Liabilities} + \text{Stockholders Equity} \]

(Riahi Belkaoui, 1992, p. 234). The equation is the fundamental part of the balance sheet and is straightforward in the way the equities and liabilities will represent the claim on the assets (Kam, 1990, p. 307). This is emphasised by previous research in the subject, which views the theory as “The rise of the corporate form of organisation” (Schroeder et al., 2001, p. 444). This went hand in hand with the separation of ownership and management which limited the liability of the owners and also resulted in the view of the company as a legal person (Schroeder et al., 2001, p. 444). The theory is more income orientated due to the view of income as the mean of meeting the owners claims. The income-statement is thereby seen as a measure of the entity’s performance and is more crucial to the shareholders since after the long term liabilities and taxes is removed, it is the income that increase the equity for the owners (Riahi Belkaoui, 1992, p. 234).

Riahi Belkaoui (1992) also discusses that the increase in owners equity cannot be seen as an income for the owners until a dividend is declared. Kam (1990) describe two views of the entity theory, the traditional view which sees equity holders as associate and accounting as a mean of report the status of their investment. The second view, is the modern view, which sees the equity holders as outsiders and the company as a firm only interested in survival and thereby sees accounting as a legal requirement and a way to keep the equity holders satisfied (Kam, 1990, p. 306).
The use of the entity theory is applicable on public companies with many owners and we believe that CDON Group AB is acting on its own for survival and to have a great output in form of income. To ease our analysis, we have throughout this thesis assumed this theory to hold. What differentiate this study from previous studies is that we are relying on the concept of the entity theory, in the area of e-commerce. Understanding the accounting theory is important, primarily the objectivity of the official financial statements and the information within. As earlier discussed we think that a focus on the income and to see the firm as a separate entity gives us the viewpoint of a relatively unbiased source of information in which the objective of the statements is to give a fair report, which goes hand in hand with the conceptual framework of IFRS (FAR Akademi, 2013, p. 9). The objective view can also be described as an ontological aspect of the entity theory, in the meaning of identify the object, or as in this study, that the entity is independent of the presence of social actors (Saunders et al., 2012, p. 131).

A connection between our assumption of the theory to hold, and our research is concerning the acquisition, and the change after the implementation of the revised IFRS 3, we see the focus on income as one source for the company to expand, and as earlier research states, an acquisition is a way to enter new markets and earn new technology and know how (Uhlenbruck et al., 2006, pp. 901-904). The assumption of the entity theory to be true will also allow the study to see the company as a separate unit from the owners, and therefore help it to limit the bias. By minimising the bias, the study argues that if the theory is true, the owners of CDON Group AB cannot affect the accounting procedure in their favour, and therefore the study argue that the theory will help the research to minimising the bias.

To conduct a massive expansion as in this case with CDON Group AB, we think that the view that the owners are outsiders and an entity acting on its best alone to survive (and expand), is the preferable path to take. The implementation of the revised IFRS 3 changes among other things how the transaction costs and consideration is treated. To implement these changes in the acquisition method, we believe that the company must be seen as an own separate entity to avoid unfair valuation and reporting.

3.1.2 Proprietary Theory

The proprietary theory is primarily taking the view of the owner and holds the owner as liable for the company’s liabilities and owner of its assets. One can see the company fully formed from the view of the owner’s interest (Kam, 1990, p. 302). The company can in this theory be explained as a financial instrument in which the owners invest capital just to increase their wealth, with this view one can think of accounting as a mean to analyse and determine the owners wealth (Kam, 1990, pp. 302-305). The theory can be explained by the following equation: Assets - Liabilities = Proprietor’s Equity. This can be seen as the assets are owned by the proprietor and the owners are liable to the debt and thereby is the equity “left” and is belonging to the stockholders (Kam, 1990, p. 303). An increase in income result in a gain in the wealth to the owners and on the flip side, an increase of expenses decline the net worth of the owners. This
means that the property of the owners is directly affected by profit or loss made by the company (Schroeder et al., 2001, p. 443).

The theory is thereby closely connected to the idea of double-entry bookkeeping and one can easily see the connection of how the net worth affected by the fact we want debit to be equal to credit and the creation of the balance sheet (Riahi Belkaoui, 1992, p. 233). The proprietary theory is best adapted on small companies with few large owners and thereby not as adaptable on CDON which is a public company with many owners (Riahi Belkaoui, 1992, p. 233). We will not use the theory further in our research but it has contributed to important developments and terminology in the area of accounting, for example is the earnings per share, dividends per share and the phrase net income for stockholders typical to the proprietary theory (Riahi Belkaoui, 1992, p. 233). In the table below, the differences between the discussed theories are summarised.

<table>
<thead>
<tr>
<th>Proprietary Theory</th>
<th>Entity Theory</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owners Viewpoint</td>
<td>Entity</td>
</tr>
<tr>
<td>Assets - Liabilities = Proprietors Equity</td>
<td>Equation</td>
</tr>
<tr>
<td>Own by Proprietor</td>
<td>Assets</td>
</tr>
<tr>
<td>Proprietor is liable</td>
<td>Liabilities</td>
</tr>
<tr>
<td>Increase in owners wealth</td>
<td>Income</td>
</tr>
<tr>
<td>Decrease in owners wealth</td>
<td>Costs</td>
</tr>
<tr>
<td>Balance Sheet</td>
<td>Focuses on</td>
</tr>
</tbody>
</table>

TABLE 1: The main differences between the Proprietary and the entity theory.

### 3.1.3 Fund Theory

According to the founder of the fund theory, William Vatter, who was against other existing theories, due to the fact that he believes that the personal element will affect the methods and valuation, used in accounting (Moonitz, 1952, p. 200). The fund theory argues that economic resources, or funds, and the business unit are considered as an economic resources (Riahi Belkaoui, 1992, p. 235). The primary focus of the fund theory is on administration and the correct use of assets (Riahi Belkaoui, 1992, p. 235). In that sense the most important parts in the financial report is the statement concerning the resources and the funds, and not the income statement or the balance sheet (Riahi Belkaoui, 1992, p. 235).
We have decided not to use the fund theory, by the reason that this theory is primarily for government or non-profit organisations, which have several branches that own separate funds (Riahi Belkaoui, 1992, p. 235). However, in the same book the author also state that this theory is relevant for organisation that accounting for bankruptcies and estates (Riahi Belkaoui, 1992, p. 236), but these factors are not applicable in our case with CDON Group AB.

### 3.1.4 Agency Theory

An agency is described as an agreement between principals and agents (Schroeder et al., 2001, p. 48). The agents primary objective is to run the entity in the most profitable way in order to increase the owners (principles) wealth. The usual reason for letting an agent act on the shareholders behalf is the scarce experience or training the shareholder possess, or that the shareholders have other occupation or is spread around the world (Schroeder et al., 2001, p. 48). When adapting the agency theory, the focus is to investigate the relationship between the parties, this can be threatening because of the limitation of control the shareholders have on the management (Schroeder et al., 2001, p. 48). This can then lead to, if there exist an unethical management, to an increase in managements wealth instead of the company's wealth, that is the stockholders (Schroeder et al., 2001, pp. 48-49). In the case of CDON Group AB which is an entity run by agents, that is the managers, and the principles, the shareholders, are limited by their shares.

Since intangibles, including goodwill, are difficult to valuate, these entries can give room for the management to be involved in earnings management (Pajunen & Saastamoinen, 2013, p. 258). However, it is the management who is most familiar with the company. Since CDON Group AB is owned by many shareholders with more or less knowledge and insight of the company, we find that to see CDON Group AB as a separate group will contribute to our research in a more favourable way. We will thereby not apply the agency theory in this study but it is an important theory to have in mind when discussing the role of management and the subjectivity as well as the transparency.
3.2 Literature Review

In this chapter we will discuss previous researches, articles and information, to confirm the gap we have discussed earlier. To be able to analyse the change of a standard and to continue on the subject and the implementation of IFRS 3. Definition of IFRS 3 is cited below:

“The purpose of this standard is to improve the relevance, reliability and comparability of the information that a reporting entity provides about a business combination and its effects in their financial reports. To achieve this, this standard establishes principles and requirements for how the acquirer:

a) in its financial statements recognises and measures the identifiable assets acquired, the received liabilities and previous non-controlled interests in the acquired company.

b) recognises and measures the goodwill acquired in the business combination or a gain from an acquisition at a low price, and

c) determines what information to disclose to enable users of its financial statements to judge the business combination’s nature and financial effects"

(Translation from: FAR Akademi, 2013, p. 130; The original can be found in Appendix 1)

In the revised IFRS 3 the acquiring company must use the acquisition method and identify the acquirer. It must also state the acquisition date and valuate the identified assets to a fair value (FAR Akademi, 2013, p. 131). One important part of the revised IFRS 3 is the valuation principle which states that the valuation of the assets and liabilities must be valued to a fair value at the acquisition date. The identification process can give rise to new assets and thereby create a higher value than the, soon to be subsidiary, has as a booked value. This is often due to intangibles as patents, brands, URL:s or a customer base that is internally developed (FAR Akademi, 2013, p. 132).

The revised IFRS 3 that was introduced in 2008, and is a part of an ongoing process from the “Annual Improvements” which comes from IASB and IFRS foundation (IFRS, 2014). Goodwill is the most discussed intangible and it can be seen as excess value from the consideration and the assets/liabilities acquired (FAR Akademi, 2013, p. 135). Goodwill can be, as discussed above, subjective and can affect earnings. The two alternatives is to account on “full” or “partial” goodwill, one can say that "full" goodwill is, since the revised standard, a possibility to use even when the acquisition is not 100 per cent (PWC, 2008, p. 11). The major difference is the proportion of the non-controlling interest, or if all non-controlling interest, is measured at its fair value at the acquisition date (PWC, 2008, p. 11). By fair value the study mean the value of the acquisition date should be as stated in IFRS 13:
“In this standard the fair value is defined as the price which at the acquisition date would be received at the sale of an asset or to be paid in a transfer of a liability through an organised transaction between the actors on the specific market”

(Translation from: FAR Akademi, 2013, p. 296; The original can be found in Appendix 1)

A first hypothesis arise from the new possibility to book a business combination, the usage of full goodwill can increase even in acquisition that is not including 100 per cent.

Hypothesis 1: The usage of full goodwill in an internet based business has increased after the implementation of the revised IFRS 3.

Further, to have the view towards the business as an entity that is liable for its liabilities and owner of its assets is not only a favourable view to have, but also mandatory when implementing the revised IFRS 3 on consolidation (PWC, 2008, p. 17). A comparison between the "old" and the revised IFRS 3 can be seen in table 2.

<table>
<thead>
<tr>
<th>International Financial Reporting Standard (IFRS) 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>&quot;Old” Standard VS Revised Standard</td>
</tr>
<tr>
<td>Transaction costs included in consideration</td>
</tr>
<tr>
<td>Consideration Transaction costs included in</td>
</tr>
<tr>
<td>income statement</td>
</tr>
<tr>
<td>Probable payment and a limited amount</td>
</tr>
<tr>
<td>Contingent consideration Payment does not</td>
</tr>
<tr>
<td>necessarily have to be probable, amount is</td>
</tr>
<tr>
<td>valued at fair value in Acquisition date, changes</td>
</tr>
<tr>
<td>is seen in income statement</td>
</tr>
<tr>
<td>Partial</td>
</tr>
<tr>
<td>Goodwill Full or Partial, company can choose</td>
</tr>
<tr>
<td>Unchanged when majority ownership received</td>
</tr>
<tr>
<td>Old interest in acquired company Valued at</td>
</tr>
<tr>
<td>Acquisition date to fair value when majority</td>
</tr>
<tr>
<td>ownership is received</td>
</tr>
</tbody>
</table>

TABLE 2: IFRS 3 before and after the change.

Since the revised standard is limiting the entity when it comes to include transaction costs in the consideration, the entities have now a possibility to book lower transaction costs in order to maintain a higher earning. Thereby can the revised IFRS 3 implies lower earnings in the income statement.

Hypothesis 2: Reported earnings has decreased after the implementation of the revised IFRS3.
One can argue that most managers believe it to be easy to make a valuation of the e-business, due to the huge amount of gathered data (Welling & White, 2008, p. 129). The responsible manager will start of by collecting data such as, the amount of visitors on the webpage, what did they look at, and the amount of sales generated from that visit (Welling & White, 2008, p. 129). Welling and White (2008) has in their study concluded that there is a positive correlation between the usage of the website and the sales (Welling & White, 2008, p. 139). However, there is no easy way of calculating the value of an e-business, and unfortunately no standards exists for measuring the impact a website have on a business (Welling & White, 2008, p. 129).

Since a lot of assets in an e-business can be seen as intangible assets and thereby can be hard to identify, we looked at previous research by Olsen & Halliwell (2007) where they discusses valuation and identification of intangibles. The authors discuss the pros and cons of identifying intangibles and putting a value on these (Olsen & Halliwell, 2007, p. 67). In the identification process there are two criteria that needs to be recognised including a legal test and a separation test, in other words if one can identify the asset apart from goodwill, and if the asset in question can be sold, rented or transferred (Olsen & Halliwell, 2007, p. 67). The asset needs to meet up to one of these criteria in order to be identified as an intangible (Olsen & Halliwell, 2007, p. 67). The authors argue for the subjectivity of valuation as a negative part of the processes and that it gives the management too much room for interpretation and once an intangible is identified and valued it must be amortised and that in its turn may affect earnings (Olsen & Halliwell, 2007, p. 67).

The authors are describing the four most common valuation techniques and these are known as; the discounted cash flow, the comparable approach, the avoided cost model and the Relief-from-Royalty (Olsen & Halliwell, 2007, pp. 67-70). The discounted cash flow, analyses the businesses estimated future cash flow, and then discount them back to present to make a good valuation on the company, it is used for wide intangibles, for example software and customer relationships (Olsen & Halliwell, 2007, p. 68). This valuation technique is one of the most common when valuation a “normal” business, that is, a business that is not an e-business.

The comparable approach, is a comparison between similar assets by creating different multiples. However, no assets are the same, therefore discounts and premiums are created, to be as fair as possible. Such discounts and/or premiums, include brand recognition, e-commerce value, pay-per-click value (Olsen & Halliwell, 2007, p. 70).

Furthermore the avoided cost approach is used to determine a value based on historical data, to perform the calculation, the company calculate on the cost avoided when acquiring an asset instead of building or create the asset in question, thereby avoid the cost (Olsen & Halliwell, 2007, p. 70).
The last approach is known as relief-from-royalty and it is a method that is taking into account the future royalties that the firm would have had to pay if they did not bought or developed the asset (Olsen & Halliwell, 2007, pp. 68-70). The method is very similar to the avoided cost model but is not using historical data, instead a royalty rate is calculated by management from the view of importance of the asset and comparison of competing assets as examples (Olsen & Halliwell, 2007, p. 68). The relief-from-royalty approach is more subjective than for example, the avoided cost approach (Olsen & Halliwell, 2007, p. 70). Recent research confirm that this valuation technique is still in use (Fuhrmann, 2013).

<table>
<thead>
<tr>
<th>Model</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>The Discounted Cash Flow</strong></td>
<td>Analyses the business’s estimated future cash flow, and then discount them back to present.</td>
</tr>
<tr>
<td><strong>The Comparable Approach</strong></td>
<td>A comparison between similar assets by developing different multiples. However, no assets are the same, therefore discounts and premiums are created, to be as fair as possible.</td>
</tr>
<tr>
<td><strong>The Avoided cost model</strong></td>
<td>To perform the calculation, the company calculates cost avoided, when acquiring an asset instead of building or creating the asset in question, thereby avoiding the cost.</td>
</tr>
<tr>
<td><strong>Relief-From-Royalty Future Cash Flow</strong></td>
<td>Is a method that is taking into account the future royalties that the firm would have had to pay if they did not buy or develop the asset.</td>
</tr>
</tbody>
</table>

TABLE 3: Models (Olsen & Halliwell, 2007, pp.68-70)

Audit research points out the issue of subjectivity, with a focus on goodwill valuation under the IFRS (Pajunen & Saastamoinen, 2013, p. 245). The company that we investigate has mandatory obligation to apply IFRS in its accounting, and the research discusses that accounting under IFRS can give opportunities for manipulation of earnings due to the problem of subjectivity (Pajunen & Saastamoinen, 2013, p. 250). In order to analyse this company we have assumed that the entity theory holds, which enables us to recognise the entity as a separate unit of transactions. Although, the subjectivity is not of importance per se, it plays a major role in the valuation of intangibles. However, Since the study applies positivism, we as researchers are value-free, and sees the collected data as the reality.
Another calculation method for the value of an online business is the Sellers Discretionary Earnings (SDE), is an approximation for what the business is worth (Shah, 2011). To calculate the approximate value of the SDE = the business income + the owners benefits + the discretionary expenses * industry specific multiplier (Shah, 2011). This valuation method is also discussed by Fuhrmann, (2013) he states that this calculation is most preferable when it is a small business, or a new internet firm in the transition of going public (Fuhrmann, 2013).

There are some factors that has to be considered during a valuation, these factors will affect the above mentioned calculations. A factor that is very important during company valuation, is if the website is unique enough, in other words, can the buyers create the website themselves or do they have to purchase the website (Bettis, 2007).

**Hypothesis 3:** The reported value of intangible assets and goodwill has increased after the implementation of the revised IFRS 3.

The third hypothesis arise since the possibility of report a lower goodwill, when transaction costs are separated, can contribute to a smaller affect in impairment testing later on. Also the fair value of intangibles has to be evaluated at the acquisition date which can affect the consideration.

Vallin et al. (2013) describe a “Six step process” to increase the value of the e-business to reach success. To distinguish the business from the rest either by product, price or brand is described in the first step (Vallin et al., 2013, pp. 172-173). Does the business have their own special and unique niche? Or does the business fight against the big giants, that already have established their businesses in the market? The value of the company will fall if it has competitors that owns the "whole" market (Bettis, 2007). About 60 per cent of the e-business that Shah (2011) has reviewed are directly affected by the competition or the unstable economy (Shah, 2011).

A good rank on the different search engines on the internet is very crucial when valuing an e-business (Bettis, 2007). This can be shown in the history, when Amazon.com was new on the market and developed an alliance with the big search engine Yahoo!, that referred any book searches to Amazon.com (Filson, 2004, p. 140). It is shown that 65 per cent of the consumers who are looking for a product, start their process in a search engine, which makes it important to be high ranked in the search results (Lantz, 2011, p. 113). The step of having a high ranking is described in the second step of Vallin et al. (2013) process list, together with good recommendation and reviews (Vallin et al., 2013, p. 173).

According to Bettis (2007), not only buildings, computers and inventory are assets, but also the URL (Bettis, 2007). The URL is not only an asset with a fixed value, the URL can itself attract customers, which will affect the sale (Bettis, 2007). A good, easy and obvious URL is important, because then you can reach even more customers and therefore also a higher value. For example, running.com is a better and a more descriptive URL than race4U2.com, and that is what Bettis (2007) calls a "keyword
URL" (Bettis, 2007). A potential buyer of an e-business will also analyse if the revenue is stable, and if there is any opportunities to expand or increase the revenues (Bettis, 2007).

Furthermore, the buyer will look at the growth of the e-company, and to back up the growth, the business must be able to show their financial statements (Bettis, 2007). A stable revenue could be connected to Vallin et al. (2013) third, fourth, fifth and sixth step in their “six step process”. The third step represents a high conversion rate, which means turning visitors to customers, the fourth step is a high average order, where they suggest customers to buy relevant products, the fifth step is to have a good delivery with a low cost, all these are directly affecting the revenue (Vallin et al., 2013, pp. 173-174). The sixth and last step is a loyalty from its customers, which indirectly lead to higher revenue, when the customers return to the store (Vallin et al., 2013, p. 174).

<table>
<thead>
<tr>
<th>“Six step process”</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1. A strong offer</strong></td>
</tr>
<tr>
<td><strong>2. Relevant traffic</strong></td>
</tr>
<tr>
<td><strong>3. High conversation rate</strong></td>
</tr>
<tr>
<td><strong>4. High average order</strong></td>
</tr>
<tr>
<td><strong>5. Effective delivery at low cost</strong></td>
</tr>
<tr>
<td><strong>6. Customer loyalty</strong></td>
</tr>
</tbody>
</table>

TABLE 4: ”Six step process” (Vallin et al., 2013, pp. 172-174)
After mentioning the valuation techniques used, and some identification methods as well as other research to have in mind when an evaluation process is in its ignition. There are reasons why a company considers or not considers to acquire another business, instead of developing and expanding new market areas and techniques themselves. For example Andrade et al. (2001) suggests that an acquisition is not that favourable when considering the change in market value of a company, which is often close to zero. King et al. (2004) shows that the acquisition is sometime even negative. Uhlenbruck et al. (2006) has performed a research on potential benefits coming from an acquisition for example, know-how and technology. The research is applicable in both online firms and offline firms (e-businesses and non-e-business). The authors discuss the advantages of an offline firm to acquire an online firm and the authors state many advantages with that kind of acquisitions for example the know-how and technology earned (Uhlenbruck et al., 2006, p. 901). The acquisitions of online firms by other online firms is more in the light of market expanding and a kind of shortcut to new markets and a larger customer base (Uhlenbruck et al., 2006, p. 903). One argument for the higher valuation of an online firm is the fact of getting to the customer base, entering new segments as well as widen the current supply. Uhlenbruck et al. (2006) states that the larger and more active online firms have a higher degree of trustworthiness which can enable consumers to pay a higher price, than if the consumers would buy the same commodity in a smaller online firm (Uhlenbruck et al., 2006, p. 904). The conclusion drawn by the authors is that an acquisition can increase value, and by expanding the customer base and trustworthiness may defend a premium price paid (Uhlenbruck et al., 2006, p. 907).
4 Results

We will structure this chapter by taking one company at a time and explaining shortly the background, before explaining the acquisition itself. First, we will analyse the acquisition of Nelly.com (NLY Scandinavia AB) and Gymgrossisten.se (Gymgrossisten Nordic AB) in 2007 and 2008 when the revised IFRS 3 was not implemented. The second part will include the acquisition of Tretti.se (Tretti AB) in 2010 and Rum21.se (Rum21 AB) in 2011 and will include the revised IFRS 3. In each one of the acquired companies we have attached the official acquisition analysis, to make it easier for you as a reader to follow our discussion.

4.1 NLY Scandinavia AB

Nelly.com was launched in Sweden in the beginning of 2003, it was the first webpage from NLY Scandinavia AB and it has since then expanded and shown a continuous growth. Later on, the introduction of NLYman.com complemented the original webpage with a larger supply of mens’ clothing. NLY Scandinavia AB has even developed their own brands and is reseller for more than 850 different brands, this makes NLY Scandinavia AB one of the major players on the online fashion market, with a vision of becoming the world's largest online fashion destination (NLY Scandinavia AB, 2014). During the year 2007 NLY Scandinavia AB was attended by CDON Group AB (Former: MTG Internet Retailing AB) who acquired 89 per cent of the stocks in August 31, 2007 (NLY Scandinavia AB, 2007, p. 2).

<table>
<thead>
<tr>
<th>NLY Scandinavia AB</th>
<th>Book value</th>
<th>Fair value adjustment</th>
<th>Recognized value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property, plant and equipment</td>
<td>365</td>
<td>365</td>
<td></td>
</tr>
<tr>
<td>Inventories</td>
<td>2,052</td>
<td>2,052</td>
<td></td>
</tr>
<tr>
<td>Trade and other receivables</td>
<td>627</td>
<td>627</td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>36</td>
<td>36</td>
<td></td>
</tr>
<tr>
<td>Deferred tax receivables</td>
<td>792</td>
<td>792</td>
<td></td>
</tr>
<tr>
<td>Trade and other payables</td>
<td>-4,260</td>
<td>-4,260</td>
<td></td>
</tr>
<tr>
<td>Net identifiable assets and liabilities</td>
<td>-388</td>
<td>-</td>
<td>-388</td>
</tr>
<tr>
<td>Goodwill on acquisition</td>
<td>14,970</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Minority</td>
<td>43</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total consideration</td>
<td>14,625</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Option acquisitions</td>
<td>-6,450</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Liquid funds in acquired companies</td>
<td>-36</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net cash outflow</td>
<td>8,139</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

TABLE 5: Acquisition analysis of NLY Scandinavia AB (Original copy from the official financial statement of CDON Group, 2009).
4.1.1. Acquisition of NLY Scandinavia AB

Nelly had some struggles from late 2006 until CDON Group AB finally completed the acquisition. The biggest complication for the small business were to combine good sales with good technology. In NLY Scandinavia AB's case, they needed pictures with zoom-function and size-guides, this would increase customer satisfaction and thus the conversion rate (Persson, 2008). The CEO of NLY Scandinavia AB believed that CDON Group AB could help them increase their conversion rate:

"- The more time we spend, the better the conversion rate will be. But you have to focus on the correct things for something to happen! Cdon knows where to focus. They know where it's worth spending the energy, says Jarno Vanhatapio."

(Translated from: Persson, 2008; The original can be found in Appendix 1)

In the Swedish business magazine "Dagens Industri" the CEO for CDON Group AB states that they believed that NLY Scandinavia AB had very good opportunities to grow both nationally and internationally (Nylander, 2007). With this acquisition CDON Group AB targeted a new market segment by include the fashion market, which CDON Group AB believed to be the new expanding online market segment (Nylander, 2007).

The acquisition of NLY Scandinavia AB was completed in August 31 2007. During that time NLY Scandinavia AB had a total sales of 15 185 654 SEK. However, due to some mistakes in the internal purchase procedure in NLY Scandinavia AB, a cost of goods sold (COGS) of -17 132 998 SEK which resulted in a major loss of -1 586 392 SEK. The loss is affecting the owners equity which ends up at -338 000 SEK, the loss is though less substantial due to a shareholder contribution of 561 000 SEK after the financial year, which mitigate the severe loss. This negative post of equity result in a negative solidity as well as a negative leverage.

In the acquisition method we can see that CDON Group AB has paid a consideration of 14 625 000 SEK for NLY Scandinavia AB and received assets and liabilities for a value of -388 000 SEK, with a minority interest of 11 per cent, this resulted in a goodwill of 14 970 000 SEK (Table 5) for the majority holder (CDON Group AB, 2009, p. 24).

There is a part of the consideration which is a contingent consideration (optional acquisition) to the last 11 per cent and it creates a liability for CDON Group AB that needs to be included in the acquisition (Nylander, 2007). A contingent consideration (optional acquisition) can be seen as a kind of insurance to the acquirer that the subsidiary, in this case NLY Scandinavia AB, fulfils the targeted objectives and thereby receives a payment in form of options, the options can change in value in the following periods, but only include the 11 per cent of the shares left (Nylander, 2007). The whole contingent consideration (optional acquisition) was finally paid 2013 (CDON Group AB 2013, p. 68).
We can see that the net cash outflow is 8 139 000 SEK after subtracting the liquid funds acquired. The question that rises is though, how CDON Group AB has evaluated the consideration to be that high (14.6 million SEK) due to the major loss of 17.9 million SEK that NLY Scandinavia AB is making. The International Accounting Standards Board (IASB) defines the valuation of high considerations and goodwill in IFRS 3:32-33, where it states that the excess value is the consideration minus the identified assets and liabilities that can be tied to the acquirer (FAR Akademi, 2013, pp. 135-136). Since this acquisition is conducted before 2010-01-01 the transaction costs is included in the consideration.

4.2 Gymgrossisten Nordic AB

Gymgrossisten was established in 1996. Gymgrossisten started their webpage in 1998, and is now the largest fitness-, health- and training-products reseller in the Scandinavian region. The company only sells through their internet web page, even internally to supply their own franchise stores. Gymgrossisten acquired bodystore.com in 2007 which contributed to an expansion towards health food and a larger customer base (Lans, 2007). During 2007 they expanded their geographical area to Finland. Currently they operate in Sweden, Finland, Denmark and Germany (Gymgrossisten, 2014).

In December 14, 2007, MTG made an offer through their subsidiary CDON Group AB to acquire Gymgrossisten (Gymgrossisten Nordic AB, 2007, p. 1).

<table>
<thead>
<tr>
<th>Net assets acquired (SEK thousands)</th>
<th>Book value</th>
<th>For value adjustment</th>
<th>Recognized total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property, plant and equipment</td>
<td>5 207</td>
<td></td>
<td>5 207</td>
</tr>
<tr>
<td>Intangible assets</td>
<td>9 041</td>
<td>60 400</td>
<td>69 441</td>
</tr>
<tr>
<td>Inventories</td>
<td>26 192</td>
<td></td>
<td>26 192</td>
</tr>
<tr>
<td>Trade and other receivables</td>
<td>7 332</td>
<td></td>
<td>7 332</td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>6 920</td>
<td></td>
<td>6 920</td>
</tr>
<tr>
<td>Deferred tax liabilities</td>
<td>-1 126</td>
<td>-16 912</td>
<td>-18 038</td>
</tr>
<tr>
<td>Trade and other payables</td>
<td>-28 843</td>
<td></td>
<td>-28 843</td>
</tr>
<tr>
<td><strong>Net identifiable assets and liabilities</strong></td>
<td><strong>24 723</strong></td>
<td><strong>43 488</strong></td>
<td><strong>68 211</strong></td>
</tr>
</tbody>
</table>

| Goodwill on acquisition            | 130 215    |
| Total consideration                | 198 426    |
| Liquid funds in acquired companies | -6 920     |
| Net cash outflow                   | 191 506    |

TABLE 6: Acquisition analysis of Gymgrossisten Nordic AB (Original copy from the official financial statement of CDON Group, 2009).
4.2.1. Acquisition of Gymgrossisten Nordic AB

The complete acquisition was done on the February 8, 2008. The consideration amounted to 198 426 000 SEK including the transaction costs of 2 000 SEK. At the time CDON Group AB (Former: MTG Internet Retailing AB) owned 99,4 per cent of Gymgrossisten Nordic AB, and in November 24, 2008, they controlled 100 per cent of Gymgrossisten Nordic AB (CDON Group AB, 2009, p. 23). Included in the Acquisition, CDON Group AB identified intangibles of 60 400 000 SEK separate from the goodwill of 130 215 000 SEK. In the post of intangibles, entries such as: Trademarks, Patents, Copyrights and Franchises could be included. Also included in the post intangibles is the entry of Brands (FAR Akademi, 2013, p. 666). With the adjustment of raising the intangible post with about 60 million SEK, CDON Group AB had to adjust the tax with 16 912 000 SEK (CDON Group AB, 2009, p. 23).

Gymgrossisten Nordic AB was at the acquisition date noted on First North (Swedish stock market) and on December 14, 2007 CDON offered 33,10 SEK for each stock in cash. The mean price before the offer was 24,00 SEK which lead to a premium of 37,6 per cent (Gymgrossisten Nordic AB, 2007, p. 1). Included in the consideration was a transaction cost of 2 000 SEK. An other important aspect to have in mind is that the acquisition of Gymgrossisten Nordic AB lead to among others a 115,000 new customers, an operating profit of 13,5 million SEK and an annual growth of 24 per cent (Holmertz, 2007).
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4.3 Rum21 AB

Rum21 started as a family business in 2006 and was in early 2011 acquired by CDON Group AB. Their market is focusing on home styling items and furniture for both private individuals as well as companies. Rum21 is an e-business that focuses on high quality and well known brands (Rum21 AB, 2014).

<table>
<thead>
<tr>
<th>Acquired net assets (£ million)</th>
<th>Carrying amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property, plant, and equipment</td>
<td>0.0</td>
</tr>
<tr>
<td>Intangible non-current assets</td>
<td>7.2</td>
</tr>
<tr>
<td>Inventory</td>
<td>1.9</td>
</tr>
<tr>
<td>Accounts receivable and other receivables</td>
<td>0.8</td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>1.4</td>
</tr>
<tr>
<td>Deferred tax liability</td>
<td>-1.9</td>
</tr>
<tr>
<td>Accounts payable and other operating liabilities</td>
<td>-2.2</td>
</tr>
<tr>
<td><strong>Net identifiable assets and liabilities</strong></td>
<td><strong>7.4</strong></td>
</tr>
<tr>
<td>Non-controlling interest</td>
<td>-1.5</td>
</tr>
<tr>
<td>Goodwill on acquisition</td>
<td>8.5</td>
</tr>
<tr>
<td><strong>Purchase price</strong></td>
<td><strong>14.1</strong></td>
</tr>
<tr>
<td>Deferred purchase price</td>
<td>-5.0</td>
</tr>
<tr>
<td>Provisions for contingent consideration</td>
<td>-2.5</td>
</tr>
<tr>
<td>Cash and cash equivalents in acquired companies</td>
<td>-1.4</td>
</tr>
<tr>
<td><strong>Net cash flow</strong></td>
<td><strong>5.8</strong></td>
</tr>
</tbody>
</table>

Transaction expenses

Transaction expenses for the acquisition of Rum21 AB amount to £0.5 million and are recognised in the item "Sales & administrative expenses" in the income statement for the Group.

Non-controlling interest

Fair value for non-controlling interest has been calculated based on purchase price paid for the acquired shares of the company.

Contingent consideration

The contingent consideration arrangement requires a conditional purchase consideration to be paid to the former owners of Rum21 AB, based on the company’s future gross profit. The conditional purchase consideration is an unlimited amount. As of 31 December, the contingent consideration decreased by £0.1 million as the probability-adjusted gross profit after a new calculation is expected to be lower than original estimates.

Note: The purchase price is rounded down in the table above, if calculate by hand it will amount to 14.2. The reason can be explained by, precautionary principle (Försiktighetsprincipen)(FAR Akademi, p. 16)

4.3.1. Acquisition of Rum21 AB

In a press-release during the time of the acquisition the CEO of CDON Group, states that the reasons for acquisition is that Rum 21 AB is an actor with a strong brand recognition in a market with a high growth (CDON Group AB, 2011b, p. 1).

The acquisition had begun in early 2011 and were fully introduced into CDON Group AB in January 31, 2011 (CDON Group AB, 2011a, p. 67). The consideration was in total 14 100 000 SEK for 90,1 per cent of the company and with a contingent consideration of 2 500 000 SEK at the acquisition, but it is changeable depending on future performance and is not necessary probable to occur. The total assets and
liabilities had a value of 7 200 000 SEK, however with a minority of 9.9 per cent the total goodwill amounts to 8 500 000 SEK for CDON Group AB. Due to the fact that CDON Group AB did not acquire the complete Rum21 AB, there is a post of minority interest of 1 500 000 SEK. They have not yet acquired the rest of the 9.9 per cent of Rum21 AB by the end of 2013.

They also have a deferred acquisition at the amount of 5 000 000 SEK. The transaction cost amounted to 500 000 SEK and is included in the income statement (CDON Group AB, 2011, pp. 68-69). The deferred acquisition was paid twice, in 2012 and was fully paid in the annual report of 2013 (CDON Group AB, 2013, p. 69). Furthermore, we can see that the contingent consideration has been paid in the official financial statements, however we cannot see if it is fully paid or not since it is dependent on performance. At the time of acquisition Rum21 AB had an operating profit of 1,1 million SEK and an annual growth in 2010 of 40% (CDON Group AB, 2011b, p.1).

This acquisition is very similar to NLY Scandinavia AB, not in the way of numbers, but in the procedure itself. However, there is one post that distinguishes itself in Rum21 AB’s acquisition, and it is the post of contingent consideration. However, it is not the number stated in the acquisition analysis that is the issue here, but the notation under the analysis, that states that the amount of the contingent consideration is unlimited (CDON Group AB, 2011a, p. 68).
### 4.4 Tretti AB

Tretti.se was established in 2004, but was not introduced on the public stock exchange market until 2005, under the name Tretti AB (Tretti AB 2014a). Tretti AB became the leading kitchen appliance e-commerce business according to Pricerunner (Tretti AB 2014b). What distinguishes Tretti AB against its competitors is the low prices and the well known brands, with a free and fast delivery (Tretti AB 2014a). Since 2011 Tretti AB is included in the CDON Group AB, when they bought 100 per cent of the company.

#### TABLE 8: Acquisition analysis of Tretti AB (Original copy from the official financial statement of CDON Group, 2012).

<table>
<thead>
<tr>
<th>Acquired net assets [SEK million]</th>
<th>Carrying amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property, plant, and equipment</td>
<td>3.1</td>
</tr>
<tr>
<td>Intangibles non-current assets</td>
<td>57.3</td>
</tr>
<tr>
<td>Financial non-current assets</td>
<td>1.8</td>
</tr>
<tr>
<td>Inventory</td>
<td>71.3</td>
</tr>
<tr>
<td>Accounts receivable and other receivables</td>
<td>16.1</td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>23.2</td>
</tr>
<tr>
<td>Deferred tax liability</td>
<td>-14.1</td>
</tr>
<tr>
<td>Accounts payable and other operating liabilities</td>
<td>-62.6</td>
</tr>
<tr>
<td><strong>Net Identifiable assets and liabilities</strong></td>
<td><strong>96.2</strong></td>
</tr>
</tbody>
</table>

**Goodwill on acquisition**

249.6

**Purchase price**

345.8

**Deferred purchase price**

-5.1

**Cash and cash equivalents in acquired companies**

-23.2

**Net cash flow**

317.5

*Transaction expenses*

Transaction costs for the acquisition of Tretti AB total SEK 4.7 million and are recognised on the "Selling and administrative expenses" line on the consolidated income statement.

The reason for acquiring Tretti AB is explained in a press release in April 28, 2011, where CDON Group AB state that Tretti AB’s strong marketshare in Sweden and their recent expansion to the nordic countries, shows a very good potential for expanding further. With the help of CDON Group AB’s knowledge, finance and the existing customer base, they can help Tretti AB reach their full potential (CDON Group AB, 2011c, p.3)

The CEO of CDON Group AB also says in the same press release that this step in CDON Group AB’s expansion, to move on to home/kitchen appliances, is in the right direction, and will give CDON Group AB the leading position in the specific market (CDON Group AB, 2011c, p.2).
In April 28, 2011, Tretti AB got an offer of acquisition from CDON Group AB, and in June 1, 2011, the consolidation was completed. During 2011 Tretti AB had sales of 535 876 000 SEK, with a total revenue of 9 886 000 SEK (Tretti AB 2011, p. 5).

CDON Group AB has paid a consideration of 345 800 000 SEK or 67,25 SEK per share, but the liabilities and assets amounts to 96 200 000 SEK, which lead to a goodwill of 249 600 000 SEK (CDON Group AB, 2012, p. 67). However, they have a deferred acquisition at the amount of 5 100 000 SEK, which CDON Group AB have not yet paid by the end of 2013. The acquisition resulted in a transaction cost which amounts to 4 700 000 SEK, which is booked in the income statement. If CDON Group AB had made the acquisition in January 1, 2011 instead of in June, they would have expected a turnover of 359 920 000 SEK, and the result amounts to 112 200 000 SEK (CDON Group AB, 2012, p. 67).

4.5 Summary of Results

In the table below is the summary of all the acquisitions mentioned above, before and after the revision of the IFRS 3. As the specific details of the differences between the acquisition is not visible to an outsider, the study will focus on the booking of the acquisition and how the procedure has changed.

<table>
<thead>
<tr>
<th>In 000SEK</th>
<th>Consideration</th>
<th>Contingent Consideration</th>
<th>Goodwill</th>
<th>Liquid founds in acquired company</th>
<th>Net cash Outflow</th>
</tr>
</thead>
<tbody>
<tr>
<td>NLY Scandinavia AB</td>
<td>14625</td>
<td>−6450</td>
<td>14970</td>
<td>−36</td>
<td>8139</td>
</tr>
<tr>
<td>Gymgrossiste n AB</td>
<td>198426</td>
<td>0</td>
<td>130215</td>
<td>−6920</td>
<td>191506</td>
</tr>
</tbody>
</table>

| Rum21 AB* | 14100 | −7500 | 8500 | −1400 | 5200 |
| Tretti AB | 345800 | −5100 | 249600 | −23200 | 317500 |

TABLE 9: Summary of results

*Note: Rum21 AB is not correct in the table due to the precautionary principle, the purchase price should be 14200 but is rounded down in the table as well as in the official financial statement (CDON Group, 2012).

One main difference between the acquisitions and the booking is that the contingent consideration seems to be higher after the revision. The question that arises is if there is an accounting procedural change or a change in the acquisition procedure.
5 Analysis of Results

We have now come to the point of analysing the results in order to answer our research question mentioned in the beginning of the paper. To continue using the structure from last chapter, we will analyse each company by itself. After the individual analysis, we continue the chapter with a larger acquisition part.

5.1 Analysis of the main acquisitions.

All acquisitions are done in a quite similar way. Therefore we want to describe the differences that we have found before and after the implementation of the revised IFRS 3.

5.1.1. Analysis of the acquisition of NLY Scandinavia AB

In this study, we analysed the official financial statement, and primarily the balance sheet of NLY Scandinavia AB from 2007, but also CDON Group’s summary of acquisitions in note 4, in CDON Group AB official financial statement from 2009.

In the above discussed acquisition of NLY Scandinavia AB by CDON Group AB we have found that the goodwill was rather high and the consideration included a contingent consideration. We think that the contingent consideration is reasonable when acquiring a company that is making a substantial loss and has a solidity that is negative and also a negative leverage. The “old” IFRS 3 states that transaction costs and changes in earn-outs (contingent consideration) will be booked against the consideration and goodwill, which seems to be followed in the acquisition of NLY Scandinavian AB (PWC, 2008, pp. 9-10). As in this situation the contingent consideration has an effect on the net cash outflow at the time of the acquisition, the possible changes that can occur later on will then have an affect on goodwill according to the earlier version of IFRS 3. This is one difference between the earlier version and the new revised IFRS 3. In the revised standard the value-change has to be declared in income statement and has an affect on earnings (PWC, 2008, pp. 9-10).

We cannot give an answer for the high goodwill during the acquisition of NLY Scandinavia AB. However, one can argue that one factor that could have had an impact on the high goodwill, were the expected growth that CDON Group AB believed that NLY Scandinavia AB could have (Bettis, 2007). This argument can be strengthen by the article by Persson (2008), where he states that NLY Scandinavia AB’s website have had several overloads, usually in combination with tv-ads. This also connects to the fact that NLY Scandinavia AB had some problems to combine the sales and the technology. This issue combined with the growth potential could be one of the main reasons why CDON Group AB saw this as an investment opportunity. By assisting NLY Scandinavia AB with the technology and in return gain a lot of customers which can be profitable for both parties.
5.1.2. Analysis of the acquisition of Gymgrossisten Nordic AB

The acquisition of Gymgrossisten Nordic AB was the largest acquisition for CDON Group AB, and the only acquisition in 2008 (CDON Group AB, 2009, p. 23). One important factor that the study identifies is the adjusted intangible asset, where CDON Group AB has raised the value by 60,4 million SEK. We believe that the reason for the increase could be that CDON Group AB has viewed Gymgrossisten Nordic AB’s acquisition of bodystore.com during 2007 (Gymgrossisten Nordic AB, 2007, p. 1) as further strengthening the brand and increased with 25,000 new customers (Lans, 2007). Furthermore, we believe and can confirm that Gymgrossisten Nordic AB want a geographical expansion, and with the help of CDON Group AB, Gymgrossisten has enhanced the opportunity to reach that goal:

“The vision is that Gymgrossisten and Bodystore shall develop via an increased product range and via a geographical expansion. CDON has a pan-nordic network for logistic and marketing that will enable a fast and cost-effective nordic launch.”

(Translated from: Gymgrossisten Nordic AB, 2007, p. 2; The original can be found in Appendix 1)

To connect the strengthening of the brand and the geographical expansion, we will discuss what we believe is the third factor of the increased intangible assets, which we would like to call the opportunity of franchise. With a strong brand, combined with a geographical expansion, more franchise stores can emerge, and therefore result in higher expected income, which we believe has increased the intangible assets post. As reported, the acquisition led to 115,000 new customers which increased the customer base substantially for CDON Group AB, this increase contributed to both Gymgrossisten Nordic AB and CDON Group AB in terms of higher relevant traffic, but we also believe that this led to a higher customer loyalty. Gymgrossisten consolidates in the concern with a previous annual growth on 24% and a high operating profit, this is also enhancing the overall performance of the firm which can contribute to higher earnings. The last recognised factor that we believed increased the intangible assets is the importance of a good rank on the search engines, such as Google and Yahoo, as confirmed by research (Bettis, 2007). On the other hand is the valuation process a discussion between the current owners and the acquirer, and to increase the value this substantial amount can not only be due to subjectivity but also the fact that the solidity was high (70 %) and a leverage that is around 1 per cent, the share had also a price to earning (P/E) of 16,79 in December 2007 (Gymgrossisten Nordic AB, 2007, pp. 5-6). We cannot find out exactly how the discussion went and what was the primarily source for this increase to the fair value, but one can see that the acquisition is, at least in terms of figures and previous results, a favourable one, and this can thereby defend a high premium. This will also strengthen the assumption on that the entity theory holds, in the way that the company act for it own gain. We think that a valuation technique that takes into consideration historical data as well as future earnings, is a probable choice to use in this valuation. Therefore we would suggest that CDON Group has used a model of
the discounted cash-flow in the acquisition of Gymgrossisten Nordic AB. In this case, we did the same analysis as in NLY Scandinavia AB, and used Gymgrossisten Nordic AB official financial statement from 2007 and primarily the balance sheet. Furthermore, we used the acquisition summary in note 4 from CDON Group AB official financial statement from 2009.

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5.1.3. Analysis of the acquisition of Rum21 AB

In the 2013 annual report CDON Group AB states that they have paid a contingent consideration amounting to 1 800 000 SEK which is based on the remaining 9.9 per cent, and evaluated at fair value to Rum21 AB. However in the statement from 2011, the contingent consideration was as high as 2 500 000 SEK. This concludes that CDON Group AB might still have a contingent consideration to pay, although the value of the contingent consideration is, as discussed, unlimited and therefore we cannot value the remaining contingent consideration, and we cannot with certainty state that it will be paid out either. This declaration of contingent consideration cannot be found in the previous acquisitions even when a contingent consideration was noted, as in the acquisition of NLY Scandinavia AB. An explanation of this is, the implementation of the revised IFRS 3 in CDON Group AB in January 1, 2010, that took place before this acquisition (CDON Group AB, 2012, p. 53). In the revised IFRS 3 the demand of how to account for contingent consideration has changed. Contingent consideration must now be valued to a fair value at the acquisition date, but does not need to be probable as the “old” standard stated (PWC, 2008, pp. 9-10). Another major difference in the way this acquisition was booked is the way in which the transaction costs are handled. In this acquisition the transaction costs amounted to 500 000 SEK and was directly booked against the income statement as a separate post (CDON Group AB, 2012, p. 66). This is also an effect of the implementation of the revised standard. The goodwill of 8.5 million SEK is arising from strategical positions, market effects and synergies (CDON Group AB, 2011a, p. 67). This is also strengthened by the comments from the CEO of CDON Group AB that confirms the acquisition as contributing to a path into a new and expanding segment, a developing brand and a positive growth (CDON Group AB, 2011b, p.1).

We have primarily used the summary of acquisition in note 5 in CDON Groups AB's official financial statement. Although, we have used Rum21 AB's own financial statement from 2010 and 2011, but only to compare the numbers with the summary found in CDON Group AB.
5.1.4. Analysis of the acquisition of Tretti AB

CDON Group AB purchased 100 per cent of Tretti AB, and therefore no minority post exists, as in the case of NLY Scandinavia AB and Rum21. In the acquisition of Tretti AB the transaction costs were excluded from the consideration, and was booked against the CDON Group AB income statement, as the revised standard states (CDON Group AB, 2012, p. 67). In contrast when we analysed the acquisition of Gymgrossisten, the study identified that the transaction cost were included in the goodwill (CDON Group AB, 2009, p. 23). Since January 1, 2010, CDON Group AB has implemented the revised IFRS 3, which implies that transaction costs should be a part of the income statement, and not included in the acquisition itself (CDON Group AB, 2012, p. 53).

During the analysis of Tretti AB, we have used both the CDON Group AB official financial statement from 2012, primarily note 5, but also Tretti AB financial statement from 2011.

This acquisition is the most expensive acquisition mentioned in this study. The reason for that could be that Tretti AB are within a market which is generally more expensive than the previous acquisitions. Also, the higher purchase price can also be explained by the recent expansion Tretti AB has done, but also the potential CDON Group AB sees in the company.

5.2 Analysis of Acquisitions

To start answering the problem statement, we first want to apply CDON Group AB's acquisitions to the previous explained differences of the “old” IFRS 3 and the revised IFRS 3. There are a few differences that this study have found and want to describe further to give the readers a greater understanding of them. The first difference, is as discussed earlier, the problem of identifying what should be included in the consideration and how the acquisition method is completed. According to the previous standard the transaction cost was a part of the consideration and booked against goodwill, which in its turn affected the net outflow. Findings of our study confirms this in the case of Gymgrossisten Nordic AB acquisition, where the transaction costs was directly included as a part of the consideration.

Before 2009 the transaction cost were included in the goodwill, and as mentioned, after the implementation of IFRS 3 from 2010-01-01 to present, the transaction costs must be included in the income statement, which lead to a decrease in revenues. With the limited data analysed, data shows that this is in line with hypothesis 2: Reported earnings has decreased after the implementation of the revised IFRS3.

Another issue is how the consideration is divided, the effect of contingent consideration, these are as we discovered in the acquisition of NLY Scandinavia AB a problem when acquire less than 100 per cent, in the previous standard the amount recognised at the acquisition had to be probable. In the revised IFRS 3 this was one major change since now the contingent consideration needs to be valued to a fair value at the acquisition
day, but can change according to the contract and the changes will only affect the earnings at the time. These changes were, as previously stated, recognised towards goodwill according to the earlier standard. Furthermore, the choice to account for “full” or “partial” goodwill is now available. This means that if the acquirer wants to buy the whole company, a “full” goodwill with the non controlling interest accounted for, can be favourable. However in case of an acquisition of less than 100 per cent the partial goodwill is more convenient, due to the increase it would contribute on the balance sheet if not used (PWC, 2008, pp. 11-12). In the acquisitions analysed in this thesis we could see that CDON Group AB has used the partial goodwill in its acquisitions, and as discussed by Lönnqvist (2012) is the non controlled interest in a public company often so small that the full goodwill approach would not be noticeable in the solidity.

During the analysis, we have not encountered the situation where CDON Group AB has had the option to choose either full or partial goodwill. According to the collected data, where only the option of partial goodwill has been use, we can neither confirm nor reject the hypothesis 1: The usage of full goodwill in an internet based business has increased after the implementation of the revised IFRS 3.

In all the four acquisitions we have analysed, we have concluded that the entry of goodwill is in most cases rather high. We cannot explain the reason for this phenomena, however, we will make an effort to pinpoint some factors that can affect this number. To be able to identify those increasing factors, we will use the above mention “Six step process” by Vallin et al. (2013). The first step, a strong offer, can be connected to the strong and well-known brands CDON Group AB are acquiring in every transaction. All the acquisitions that we have analysed had a recognised brand and a stable customer base before CDON Group AB made the offer. For example, NLY Scandinavia AB had before the acquisition increased their sales with 50 per cent, but also expanded their supply of new fashion brands. Similar pattern is found in the other acquisitions mentioned above. This fact, we believe, made the consideration as well as the value, to increase. The second step, relevant traffic, is connected to the first step, in terms of the importance of a high valued brand. The traffic to the acquired company’s homepage is controlled by the different search engines, good recommendations and reviews, which describes a good and reliable brand. As described in step one, CDON Group AB has acquired well-known brands only. Before the acquisition of Gymgrossisten Nordic AB, who recently had acquired bodystore.com, this implied that the relevant traffic had increased, which then might had lead to a higher value. The several overloads on NLY Scandinavia AB’s webpage also indicates a very high traffic, and thus might lead to potential a higher value. Tretti AB and Rum21 AB was both on a high growth path and the relevant traffic can thereby be a crucial factor for the timing of the acquisition (CDON Group AB, 2011c, p.3; CDON Group AB, 2011b, p. 1).

The brands and the high traffic is relating to the acquired businesses, one can thereby reason for the third hypothesis stated in this thesis: The reported value of intangible assets and goodwill has increased after the implementation of the revised IFRS 3.
In the analysed acquisitions there is no indications on a higher value on reported intangible assets, the considerations is in sober relation to the company acquired, we can thereby according to results reject this hypothesis.

Since all the acquisitions made by CDON Group AB, have been well known brands before the transaction and with a strong customer base, the acquired companies can have the best and lowest offers on the market. This relates to the third step, high conversion rate, which is about the “power of offer” (Vallin et al., 2013, p. 173). After CDON Group AB acquired NLY Scandinavia, the first priority was to build a new version of NLY Scandinavia AB’s webpage, to be able to turn more visitors to customers (Persson, 2008). An example of that is the fact that the payment procedure has been shortened from five steps to only one step (Persson, 2008).

The fourth step, high average order, is a step that we do not have the ability to analyse since that would have demanded us to look at CDON Group’s or its acquired companies order statistics. The same applies for step five, effective delivery at low cost, which demands us to go back and see what CDON Group AB and its acquired companies had for a delivery policy before and during the acquisition. One thing to bear in mind is that CDON Group AB has bought a logistic company in 2012 to increase the effectiveness of delivery and to have the skills necessary in house, in order to enhance the customer experience (CDON Group AB, 2012, p. 1).

Customer loyalty, is the sixth and last step of the “Six step process” explained by Vallin et al. (2013). It is connected to the first three steps, again with the common variable of the brand. With the strong brand and the large customer base the acquired companies had during the acquisition, we believe that there existed a large group of loyal customers in the acquired company, which then indirectly were transferred to the CDON Group AB. One thing that also contribute, is the fact that CDON Group AB has kept the original website and names of the acquired companies, and therefore the costumers can recognise themselves and the loyalty can maintain the same. As research in the field states (Uhlenbruck et al., 2006, p. 904); customer loyalty and customer base is crucial factors to have in mind when studying and discussing an e-business, the strong recognition and loyalty can make customers to pay a higher price for the same object (Uhlenbruck et al., 2006, p. 904). As the group expands its customer base is increasing, this implies a higher value for the group and may contribute to a more loyal customer base (Uhlenbruck et al., 2006, p. 904).

One important factor that Vallin et al. (2013) is not mentioning, and that we want to enlighten is the fact of an increase in value due to a possible expansion and/or a possible grow in the revenue. In all the acquisitions, the most probable reason, and what we believe to be CDON Group AB’s reason for acquiring the companies, is that they see a growing potential. CDON Group AB acquires NLY Scandinavia AB to be able to expand their market in fashion, but also because they saw the potential of the website. In the case of Gymgrossisten, CDON Group AB had increased the intangible assets by 60 million SEK, and we believe that the large increase could have had its reason in the ambition Gymgrossisten had of expanding on the geographical market. Even in the case...
of Rum21 AB the management saw a growing potential in a lucrative market (CDON
Group AB, 2011b, p.1). It was the potential to grow in another new market that made
CDON Group to acquire Tretti AB. Tretti AB had a large amount of costumers and had
a strong position on the Swedish market (CDON Group AB, 2011c, p.3). The reasons
for the acquisitions by CDON Group AB can be defended by the article by Bettis
(2007), where he state that the purchaser would look for opportunities to expand the
planned acquired company.

CDON Group AB states in their official financial statement that they are valuing their
intangibles by using the discounted cash flow model, which is based on growth,
earnings and historical data on both the actual item and market-development. The
projected cash flow is based on the last five years and is individually projected due to
costs and risk (CDON Group AB, 2009, p. 30). After that CDON Group AB develops an
appropriate discount rate and uses it to give a fair present value (CDON Group AB,
2009, p. 30). The technique for valuation according to IFRS 3 is the recognition to fair
value, which is defined in IFRS 13 as well in section 2.2 and is only interested in the
actual value that would occur in a transaction of the specific asset or liability (FAR
akademi, 2013, p. 296).

Since CDON Group AB has stated in their official financial statement that they are
basing their intangibles on the discounted cash flow model. When analysing the latest
official financial statement from 2013, in note 10 “Intangible non-current assets”, and
by analysing every official financial statement from the year 2007 to 2013 we can see
that there has not been any changes of valuing the intangibles (CDON Group AB, 2013,
p. 73). The valuation of intangibles has according to our analyse not changed in the
reporting procedure, but if the underlying procedure of valuation of both intangibles and
acquisitions has changed, apart from what the official financial statements tells us is a
matter of further research. The positivistic philosophy enables us to see the figures and
numbers as reality, and thus gives us the means to analyse these as true. Our research
questions, thereby if the revision of the IFRS 3 has resulted in a valuation procedural
change or if its implementation is a matter of a reporting procedural change. The study
identifies the reporting as an instrument of revealing a state of development in a
company, and to be able to implement a change of the reporting, it is of crucial nature to
see the entity as a separate unit to avoid subjectivity. This conclusion contributes to the
entity theory in a clear and visible manner.

The factor of the subjectivism, mention by Pajunen and Saastamoinen (2013), must be
mentioned, and whether the management has made a higher valuation to increase their
own wealth, or if the management has acted in good faith against the company. We do
not have the resources, time and influence to conclude a straight answer that is closest to
the reality. To find a correct answer on how they have valued the consideration, we
would have to conduct interviews with the responsible managers. However, even if we
had the time to conduct the interview, we believe that the process of valuing of a
company is classified business information, that the study could not have been allowed
to receive.
Since CDON Group AB is a public company and one of Sweden's largest internet retailers, we believe that seeing it as one company which own its assets, helps us to analyse and conduct this research. Therefore, the entity theory was assumed to be true throughout our study. The assumption of entity theory can help us to gain an understanding in the analysis of the acquisition and how the managers is acting for the company’s best interest and how they are using the assets. It is important that management is using the assets for the company's best interest in order to have a high growth and to increase the revenues. In the analysed acquisitions we cannot see any major differences between the procedure of the acquisitions or the reporting. Although, the rules have changed, the valuation procedures seems to be unchanged.

To see the change of IFRS 3 in a positivistic view, we have seen the fact within the financial statement as true, and reflecting the reality. We have seen that the numbers have not changed, been removed or added, when IFRS 3 changed, the numbers have only been moved to another entry and/or in another part of the financial statement. These differences have affected the reported income in a way, as in line with hypothesis 2, but how much this affect the decisions regarding acquisitions cannot data reveal. By applying the philosophy of positivism, this research is able to see the numbers, that is, the changes from the old to the revised IFRS 3 to be real. Furthermore, by assuming that the theory of entity to hold, gives the research probable causes to state that the values in the statements has been evaluated to a true value and has not been tampered with.

<table>
<thead>
<tr>
<th>International Financial Reporting Standard (IFRS) 3</th>
<th>&quot;Old Standard&quot;</th>
<th>VS</th>
<th>Revised Standard</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>NLY Scandinavia AB</strong></td>
<td>Acquired 100 per cent.</td>
<td>Consideration</td>
<td>A contingent consideration is included.</td>
</tr>
<tr>
<td><strong>Gymgrossisten AB</strong></td>
<td>None</td>
<td>Contingent consideration</td>
<td>The contingent consideration is unlimited in its value, and do not have to be probable.</td>
</tr>
<tr>
<td><strong>Rum 21 AB</strong></td>
<td>The goodwill was in line with their expectations</td>
<td>Goodwill</td>
<td>Partial Goodwill is reported in the official financial statement.</td>
</tr>
<tr>
<td><strong>Tretti AB</strong></td>
<td>Transaction cost included in the consideration.</td>
<td>Transaction costs</td>
<td>Transaction costs booked in income statement.</td>
</tr>
</tbody>
</table>

TABLE 10: Comparison IFRS 3
6. Conclusion

This study has discussed the change of a revised standard and how it has affected online business valuation and reporting issues during mergers and acquisitions. As stated in the problem background the revision of a standard and its effects on the parent company’s accounting procedure are in focus in this thesis. We have analysed archival data and drawn conclusions to give an answer to our problem statement: Has the implementation of the revised IFRS 3 changed the reporting procedures in how a listed e-business acquires another e-business?

To give an answer to this question we have used a mixed method data collection to retrieve both numerical data and textual information from official financial statements and similar articles and press releases. This study have assumed the entity theory to be true and applied the philosophy of positivism. The theoretical approach combined with the philosophical standpoint enables us to see the changes that occurred in the light of the entity theory.

The revised IFRS 3 is a regulation which demands a higher transparency, explanation of the acquisition, as well as a change in consideration identification. This change has affected the reporting in acquisitions in which we can identify in the acquisition method. However, the changes we can see could also arise from a different way of reporting and not from real numbers. By assuming the entity theory to be true, the study can see a management acting for the company’s interests and use the assets in a favourable way. Furthermore, we can identify the different acquisitions as separate events of expansion, and the reporting as a tool for the management to describe the event. To change the event of expansion, would demand extensive work and be resource demanding, to change the describing tool for reporting the event would not be as resource demanding. We can therefore draw the conclusion that it is substantially less effortless to change the tool than the procedure.

To continue and give an answer on our problem statement, if the revised IFRS 3 has changed the reporting procedure in how an e-business acquire another, we can in a reporting point of view see a difference in the acquisition in terms of identification of consideration and the description of the acquisition. The change in contingent consideration value is also identified in the revised standard.

Findings of this thesis contribute to the entity theory by showing if IFRS 3 revised, are used as a tool for guidance of accounting, and not used as a regulation that require a change in procedure. Furthermore, this study has found that the reporting is different and it has strong evidence for that the difference is due to the change of reporting standards.
The study is not able to answer if the revision is changing the whole acquisition procedure or if it is the reporting procedure that is the subject for transformation.

Reliability in analysing acquisitions as an outsider of the company and without a proper influence within the company, is reach by relying on official documents and figures. This has been a challenge in this thesis. As we have discussed, the revised IFRS 3 changed how to account for acquisitions. How the underlying valuation procedures have taken place, however, it is not straightforward to analyse, when comparing accounting information in official financial reports. The thesis can though identify a change in reporting procedure, the booking of the figures has changed and the direct effect on income can be visible, though the underlying figures is not visible in the financial statements. These underlying figures will always be there, regardless of our analysis and the framework of the standards, however, since we have applied the positivistic view in this research, we will ignore this, and assume that the numbers we see are the real ones.

The study has analysed the CDON Group AB's financial statement in the framework of the entity theory, that is, to analyse the hard facts without to much concern of the background of the facts. In other words, we have analysed the financial statements as an unbiased source of the companies financial position. We, of course, did have the concern of the background in our mind throughout the thesis. However, we have not received a reliable answer of how the management were able to conclude the numbers. Furthermore, by assuming the entity theory to hold, the study were able to use the facts and assume that these official numbers are also the real numbers used for the company’s best interest. Since we have analysed the largest e-company in Sweden, we can say that there is a high likelihood that these results can be generalised in most Swedish e-companies.
7. Recommendation for future research

With this thesis we would like to give a deeper understanding of how the development and implementation of IFRS 3 has influenced the accounting of an online business. In the work with this research we have developed questions and thoughts that we think could be interesting to investigate further. The IASB as a standard setter is constantly developing and managing the standard, and to investigate a revision of an established standard has been interesting. We think that one subject for future research is to see how a non-e-business is affected, in terms of profit and loss, from acquiring an e-business. Also a further examination of how the concerned parties think when evaluating acquisitions of other e-businesses in a qualitative research design with an abductive or inductive approach would have been an interesting continuation on our research. These are good examples of subjects for a future master thesis or degree project.

8. Ethical and social issues

Based on the fact that we have used figures from a public listed company, which are obliged to follow certain accounting rules and standards, IFRS, we argue that we do not have any ethical issues regarding our retrieved data. Furthermore, in Sweden, all documents regarding a listed company's financial situation are available to the public. Therefore, our study does not include any classified information that can harm a third party.

The revision of an accounting standard have an affect on the accounting procedure and this will affect companies that uses the IFRS. If the change is substantial, the affect will also be substantial, this can reduce earnings and thereby effect both owners and employees. The effect also occurs if the changes is very complex, the need for auditors becomes more important and contributes to a higher cost. If large companies is reducing their earnings due to a procedural change, the investors in those companies will draw back their investments and on the far end the social system (pension founds , etc.) will experience a downfall.
9. Acknowledgement

In the process of making this research, the division of work has been divided equally between the authors. We have revised our timetable over time, due to delays and corrections beyond our control. Although the work has proceeded according to plan, we have found the subject interesting and we have developed a knowledge and an understanding of the International Financial Reporting Standards and how those are used in a public traded company. We have also gained a knowledge in how a revised standard can be implemented and how it can be identified in a financial reports.

During our last editing of this study, CDON Group AB has divested Rum21 AB on the 22 May, 2014. The acquirer was Royal design Group and the consideration amounted to 68 000 000 SEK (CDON Group AB, 2014b). Since the consideration for CDON Group AB when they acquired Rum21 AB was 14 100 000 SEK, we can see that the business has increased in value since CDON Group AB acquired Rum21 AB in 2011.
10. Reference List


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http://web.retriever-info.com/services/businessinfo/displayBusinessInfo?orgnum=5566906987  
[Retrieved: April 28, 2014]


APPENDIX 1: Translations

IFRS 3, definition

Syftet med denna standard är att förbättra relevansen, tillförlitligheten och jämförbarheten på den information som ett rapporterande företag tillhandahåller om ett rörelseförvärv och dess effekter i sina finansiella rapporter. För att uppnå detta fastställs i denna standard principer och krav för hur förvärvaren:

a) i sina finansiella rapporter redovisar och värderar de identifierbara förvärvade tillgångarna, de övertagna skulderna och eventuella innehav utan bestämmande inflytande i det förvärvade företaget

b) redovisar och värderar den goodwill som förvärvas i rörelseförvärvet eller en vinst vid ett förvärv till lågt pris, och

c) fastställer vilka upplysningar som ska lämnas för att möjligöra för användare av de finansiella rapporterna att bedöma rörelseförvärvets karakter och finansiella effekter.

(IFAR Akademi, 2013, p. 130)

IFRS 13, definition

I denna standard definieras verkligt värde som det pris som vid värderingstidpunkten skulle erhållas vid försäljning av en tillgång eller betalas vid överlåtelse av en skuld genom en ordnad transaktion mellan marknadsaktörer

(IFAR Akademi, 2013, p. 296)

Draghjälp för Nelly, quotation original

"- Ju mer tid vi lägger ner, desto bättre conversion rate. Men det gäller att fila på rätt ställe för att det ska hända något! Cdon vet var man ska fila. De vet var det är värt att lägga energin, säger Jarno Vanhatapio."

(Persson, 2008)

Gymgrossisten, quotation original

“Visionen är att Gymgrossisten och Bodystore ska utvecklas via ett utökat produktutbud samt via geografisk expansion. CDON har ett pan-nordiskt nätverk för logistik och marknadsföring som möjliggör en snabb och kostnadseffektiv nordisk lansering.”

(Gymgrossisten Nordic AB, 2007, p. 2)
# APPENDIX 2: Literature search

Keyword use in our literature search:

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<th>Limitations</th>
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<th>Selected</th>
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<tr>
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<td>1</td>
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<tr>
<td>Darren Filson</td>
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<td></td>
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</tbody>
</table>

**Google Scholar Database**

valuation + e-business + acquisition                    | 2006>2014                    | 8270  | 3        | 1        |