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Australian Accounting Standards Board

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Mr Wayne Upton
Chairman
IFRS Interpretations Committee
30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Dear Wayne

Clarification of accounting for a business combination achieved by contract alone

We are writing to seek clarification of the IFRS Interpretation Committee's position on the interaction of the IFRS 3 *Business Combinations* requirement for entities to identify an acquirer, with the requirement in IFRS 10 *Consolidated Financial Statements* for entities to prepare consolidated financial statements when control exists.

Specifically, we are seeking clarification as to whether, in circumstances where an acquirer has been identified for a business combination achieved by contract alone, such as in a stapling arrangement, with no entity/party to the business combination having 'control' over the other entities, the 'acquirer' is the parent for the purposes of preparing consolidated financial statements under IFRS 10.

Consistent with the Committee's process for considering issues, we have provided a more detailed explanation of the issue, possible alternative accounting treatments and reasons for the Committee to address this issue as a potential agenda request in Appendix A to this letter.

We seek your clarification on this issue urgently to help avoid diversity in practice arising on this issue in financial statements for the period ending 31 December 2013.

If you require further information on the matters raised above or in Appendix A, please contact me or Kala Kandiah (kkandiah@aasb.gov.au).

Yours sincerely

K.M. Stevenson

Kevin M. Stevenson
Chairman and CEO

Appendix A: Potential agenda item request

When two or more entities and their businesses are brought together by contract alone, with no transfer of consideration or exchange of equity interests, the combination is accounted for as a business combination, where an acquirer is identified and the acquisition method of accounting is applied, even in circumstances where no entity/party to the business combination has 'control' over the other entity/entities. . This approach is based on the following guidance in IFRS 3:

- paragraph 43 "An acquirer sometimes obtains control of an acquiree without transferring consideration. The acquisition method of accounting for a business combination applies to those combinations. Such circumstances include*:*

  ...

  (c) The acquirer and acquiree agree to combine their businesses by contract alone. The acquirer transfers no consideration in exchange for control of an acquiree and holds no equity interests in the acquiree, either on the acquisition date or previously. Examples of business combinations achieved by contract alone include bringing two businesses together in a stapling arrangement or forming a dual listed corporation";

- the definition of business combination in Appendix A "….Transactions sometimes referred to as 'true mergers' or 'mergers of equals' are also business combinations as that term is used in this Standard"; and

- paragraph 6 "For each business combination, one of the combining entities shall be identified as the acquirer. … If a business combination has occurred but applying the guidance in IFRS 10 does not clearly indicate which of the combining entities is the acquirer, the factors in paragraphs B14-B18 shall be considered in making that determination."

As mentioned in paragraph 43(c) of IFRS 3, a stapling arrangement is an example of a business combination achieved by contract alone. A stapling arrangement is a contractual arrangement between two or more entities or their shareholders, typically without the transfer of consideration, where the equity securities of the entities in a stapling arrangement are stapled together and the entities each have the same owners. The stapled securities are quoted as a single security and cannot be traded or transferred independently. Generally a stapling transaction is entered into for tax reasons and in many of these arrangements, no entity/party to the stapling arrangement has 'control' over the other entities.

Question

Where an acquirer has been identified for a business combination achieved by contract alone, such as in a stapling arrangement, with no entity/party to the business combination having 'control' over the other entities, is the 'acquirer' the parent for the purposes of preparing consolidated financial statements under IFRS 10?

We are aware of two views on the issue:

View 1

If a business combination has been achieved by contract alone between two or more entities, with no entity having control, IFRS 3 paragraph 6 requires one of the entities to be identified as the acquirer for the purposes of acquisition accounting. That same entity would be identified as the parent for the purposes of preparing consolidated financial statements under IFRS 10.

In other words, there is no need to go through the criteria in paragraph 7 of IFRS 10 to determine the parent entity for a business combination achieved by contract alone where in substance there is no control by one entity over the others. In such circumstances, the acquirer identified in accordance with the guidance in paragraph B14–B18 of IFRS 3 would be the parent for the purposes of preparing consolidated financial statements in accordance with IFRS 10.

View 2

IFRS 10 requires an entity that is a parent to present consolidated financial statements. IFRS 10 defines a parent as an entity that controls one or more other entities. For the purposes of IFRS 10, an investor controls an investee if and only if the investor has all of the following:

(a) power over the investee;
(b) exposure, or rights, to variable returns from its involvement with the investee; and
(c) the ability to use its power over the investee to affect the amount of the investor's returns.

In a business combination achieved by contract alone where there is no controlling entity, the acquirer identified under IFRS 3 would not necessarily be the parent under IFRS 10. 'Control' and 'parent' would need to be identified based on the guidance in IFRS 10 and if there is no control, there would be no parent entity identified under IFRS 10 and consolidated financial statements cannot be presented.

Reasons for IFRS IC to address the issue

Criteria	**Assessment**
The issue is widespread and has practical relevance.	Yes – Business combinations achieved by contract alone are relatively common in many parts of the world. Examples of such business combinations are stapling arrangements (prevalent in Australia and Canada) and forming dual listed entities (such entities exist in Europe and Australia). In most such business combinations, there is no controlling entity/party.
The issue indicates that there are significantly emerging divergent interpretations in practice.	Yes – IFRS 10 is applicable from 1 January 2013 and we are currently aware of divergent views on the issue as articulated above.

Financial reporting would be improved through the elimination of the diversity.	Yes – reducing diversity on this issue would help comparability of financial statements, particularly as the diverse views on this issue would result in completely different sets of financial statements.
The issue is a narrow implementation or application issue that can be resolved efficiently within the confines of existing IFRSs and the *Framework for the Preparation and Presentation of Financial Statements*, but not so narrow that it is inefficient to apply the interpretation process.	Yes – it requires a clarification of whether the acquirer identified in accordance with IFRS 3 for business combinations achieved by contract alone (with no controlling entity/party) would be the parent entity for the purposes of preparing consolidated financial statements under IFRS 10.
If the issue relates to a current or planned IASB project, there is a pressing need to provide guidance on a more timely basis than would be expected from that project.	There is no current relevant IASB project (on the active or research work plans).