



REDOVISNINGSRÅDET

09 July 2004

Sir David Tweedie
International Accounting Standards Board
30 Cannon Street
London
ED4M 6XH
United Kingdom

Dear David,

**Re: Exposure Draft of proposed Amendments to IFRS 3 Business Combinations
Combinations by Contract Alone or Involving Mutual Entities**

- 1 We appreciate the opportunity to respond to the International Accounting Standards Board's above-mentioned exposure draft. The response in this letter represents the view of The Swedish Financial Accounting Standards Council.
- 2 The exposure draft deals with combinations in which separate entities are brought together to form a reporting entity by contract alone without the obtaining of an ownership interest and with combinations involving two or more mutual entities. We understand that the objective of the exposure draft is to avoid the continued application to such combinations of either the pooling of interests method or the purchase method, as defined in IAS 22 *Business Combinations*, until the issue has been fully studied in phase 2 of the Business Combinations project.
- 3 We note that the amendments in the exposure draft are intended to apply already as from 31 March 2004, that is, from an even earlier date than the point in time at which the exposure draft was issued. According to our opinion, this gives rise to distinct uncertainty regarding the appropriateness of the suggested amendments.
- 4 From a practical point of view, the intention that the amendments should apply already as from 31 March 2004 implies that an entity presently engaged in negotiations concerning a business combination cannot actually be certain which rules apply for the accounting of the combination. We regard this as an extremely unfavourable situation, which could cause serious problems for the entities concerned.
- 5 From a principle point of view, the retrospective application implies a fundamental departure from the Board's general policy that amendments to the standards should be published a number of months prior to their application. This is also an obvious departure from IASB's recent declaration of a 21-month "calm period", starting from April 2004, and the ambition to create a stable platform for the financial reporting.

- 6 We find it most important that amendments to existing standards, that are going to be applied shortly after their publication, and in extreme cases even before their publication, are kept at an absolute minimum and only introduced when there is a need to solve serious problems requiring immediate attention.
- 7 We cannot see that this is the case with respect to the amendments in the exposure draft. It is true that it would be unfavourable to retain IAS 22 until the issue in question has been fully studied in phase 2 of the Business Combinations project. This is especially unfavourable as regards retaining the pooling of interests method as an accepted method, when applicable, for the types of business combinations in question, while the method is, at the same time, forbidden for all other types of business combinations. We also understand that it would be confusing to have two different versions of the purchase method in force at the same time. However, we cannot see that this is a problem of such a magnitude and urgency that it justifies the serious disadvantages of a retroactive application of the amendments, as commented upon above.
- 8 We would also like to underline that the solution presented in the exposure draft has serious shortcomings. As stated in BC 7, it is difficult to make all business combinations in question fall into the pattern of the purchase method. This is evidenced by the fact that it is often difficult to identify the acquirer and that it is difficult to measure the consideration reliably, both of which are cornerstones of the purchase method. We note that the rules in the exposure draft for the application of the purchase method differ from the corresponding rules in IFRS 3. This will evidently reduce the comparability between the types of business combinations addressed in the exposure draft and other business combinations.
- 9 The solution presented in the exposure draft will most probably be of an interim character as the issue will be studied in more depth in phase 2 of the Business Combinations project when, we assume, the above-mentioned deficiencies will be analysed and when, also, the fresh start method will be studied. The problem addressed in the exposure draft is, therefore, likely to disappear in a few years' time.
- 10 We have, therefore, come to the conclusion that the amendments in the exposure draft whilst eliminating one unfavourable situation, namely, the retention of IAS 22 until phase 2 of the Business Combinations project is finalised, would replace it with another situation that is far from favourable. The net effect of the amendments would, therefore, according to our opinion, not be sufficient to justify the problems caused by a retrospective application of the amendments in the exposure draft.
- 11 *Based upon the above-mentioned considerations, we are of the opinion that the exposure draft should not lead to any amendments to IFRS 3.*

Question 1

The Exposure Draft proposes:

- (a) *to remove from IFRS 3 the scope exclusions for business combinations involving two or more mutual entities and business combinations in which separate entities are brought together to form a reporting entity by contract alone without the obtaining of an ownership interest.*
- (b) *to require the acquirer to measure the cost of a business combination as:*
- (i) *the aggregate of the following amounts when the combination is one in which the acquirer and acquiree are both mutual entities:*
 - *the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities; and*

- *the fair value, at the date of exchange, of any assets given, liabilities incurred or assumed, or equity instruments issued by the acquirer in exchange for control of the acquiree.*

Therefore, goodwill would be recognised in the accounting for such transactions only to the extent of any consideration given by the acquirer in exchange for control of the acquiree.

- (ii) *the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities when the combination is one in which separate entities or businesses are brought together to form a reporting entity by contract alone without the obtaining of an ownership interest. Therefore, no goodwill would arise in the accounting for such transactions.*

Is this an appropriate interim solution to the accounting for such transactions until the Board develops guidance on applying the purchase method to such transactions as part of a subsequent phase of its Business Combinations project? If not, what other approach would you recommend as an interim solution to the accounting for such transactions, and why?

Response

12 No.

13 Instead, for the reasons mentioned above, the two types of business combinations dealt with in the exposure draft should continue to be accounted for according to IAS 22 until the Board, in the second phase of the Business Combinations project, develops guidance for such transactions.

14 We would also like to mention that we have noted that no explanation is given in the Basis for Conclusions in the exposure draft regarding the different treatment of costs directly attributable to the combination according to paragraphs 24(b) and 31B.

Question 2

The Exposure Draft proposes that no amendments be made to the transitional and effective date requirements in IFRS 3. This would have the effects set out in paragraph 6(a)-(c) above on the accounting for business combinations in which the acquirer and acquiree are both mutual entities or in which separate entities or businesses are brought together to form a reporting entity by contract alone without the obtaining of an ownership interest.

Is this appropriate? If not, what transitional and effective date arrangements would you recommend for such business combinations, and why?

Response

15 According to our opinion, the exposure draft should not lead to any amendments in IFRS 3. Therefore, a response to Question 2 is not applicable in our case.

Yours sincerely,

The Swedish Financial Accounting Standards Council

Dennis Svensson

Managing Director