

[PN 71]

Practice Note 71

Financial reporting by Australian entities in dual-listed company arrangements

Chapter 2M — Financial reporting and audit

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Introduction

[PN 71.1] ASIC has been approached by Australian companies considering proposals to enter into “dual-listed company” (“DLC”) arrangements. These companies have sought ASIC’s views as to the appropriate accounting treatment to be adopted by them under such structures.

[PN 71.2] ASIC has asked the AASB to develop rules to clarify the accounting treatment of DLC structures as a matter of urgency. However, the AASB may not be able to make a decision on this matter in the near future. In the meantime, ASIC considers it necessary to express its views as to how it expects the existing requirements of the Corporations Act and accounting standards to be applied to these structures. The operation of this practice note will be reviewed in light of any accounting standard that becomes operative which deals with financial reporting by companies in DLC structures.

[PN 71.3] The key features of the DLC structure proposals put to ASIC are summarised in the attachment to this practice note. ASIC has considered the features described in the attachment in preparing this practice note.

Acquisition accounting and consolidation

[PN 71.4] The manner in which AASB 1015 “Acquisitions of Assets” and AASB 1024 “Consolidated Accounts” apply in relation to DLC structures is unclear.

[PN 71.5] It is clear, however, that AASB 1015 and AASB 1024 are intended to deal with transactions that are, in substance, acquisitions or give rise to control of one entity by another.

[PN 71.6] ASIC considers that certain DLC transactions and structures may give rise to acquisitions in substance, notwithstanding their form.

[PN 71.7] There are various factors that ASIC is likely to take into account in determining whether a DLC structure involves an acquisition in substance or control by one entity over the other.

[PN 71.8] For example, ASIC considers that there is likely to have been an acquisition, and that control is likely to have arisen, if:

- (a) each company does not retain its legal identity, or assets and businesses are transferred between the two companies for values other than fair values (except for transfers necessary for dividend equalisation purposes);
- (b) there is a change in the respective shareholders of each company as a result of entering into the DLC arrangement (although special shares may be held by a special purpose trustee or nominee vehicles to achieve a sharing of certain voting rights between the shareholder groups);
- (c) each company does not have a primary listing in a different country and does not retain that listing after creation of the DLC structure;
- (d) the companies do not have separate boards appointed at their respective general meetings (although the boards may have common directors);
- (e) each board does not separately approve the appointment of any common key management staff holding positions across both entities;
- (f) each company does not separately declare its own dividends and any changes in share capital;
- (g) the shareholders of either company do not retain the right to terminate the DLC structure at any time without any significant penalty, at a meeting of the company at which the shareholders of the other company have no voting rights on any resolution to effect such a termination, subject to such termination also being separately agreed to by the shareholders of the other company in a similar manner at a meeting of the other company;

- (h) there are significant direct or indirect shareholdings by one entity in the other;
- (i) one entity (as opposed to its shareholders) has a contractual right or capacity to control, veto or override decisions of the board or shareholders of the other entity;
- (j) there are arrangements whereby the activities of one of the entities are predetermined by agreement (refer also UIG Abstract 28 “Consolidation — Special Purpose Entities”); or
- (k) other circumstances exist that give rise to rights or capacities in one entity (as opposed to its shareholders) to control, veto or override decisions of the board or shareholders of the other entity.

[PN 71.9] Should any of the factors detailed in [PN 71.8] arise subsequent to the creation of a DLC structure, that could trigger acquisition accounting and control at that time.

[PN 71.10] ASIC also considers that there is likely to have been an acquisition, and that control is likely to have arisen where there is a significant disparity in the relative sizes of the combining entities. As a guide, where the fair value of one of the entities is more than 1.5 times the fair value of the other entity (ie the first entity’s fair value represents 60% or more of the combined fair value) at the time the DLC is created, ASIC will usually take the view, for Australian reporting purposes, that the larger entity should be regarded, in substance, as having acquired the smaller. In an arm’s-length transaction, the equalisation ratio should generally be used as the basis for determining the relative fair values of the entities, rather than the relative market capitalisations of the entities or another measure.

[PN 71.11] Where there is an acquisition in substance, ASIC considers that AASB 1015 and AASB 1024, and all the relevant requirements of those standards, should be applied to the DLC transaction and structure in accordance with the terms of those standards, and ASIC will be unlikely to give any relief from the terms of those standards.

[PN 71.12] ASIC’s response in any particular case will be based on the facts as provided to us. In any particular situation, there may be other factors that have not been considered above that could lead us to the view that there is control for the purposes of AASB 1024 and possibly also an acquisition for the purposes of AASB 1015.

Other reporting requirements

[PN 71.13] If there is no acquisition or control, ASIC would expect that combined financial reports for the entities concerned will be included as a note to their financial statements in order to give a true and fair view of their consolidated and single entity financial statements. We may consider relief for a format that gives a clearer presentation to users of the financial report.

[PN 71.14] Given the nature of the DLC arrangements, ASIC would expect the combined financial report to be included as a note to the financial statements of the listed Australian entity, even if the foreign entity is considered to be the controlling entity and prepares consolidated financial statements in its place of origin.

[PN 71.15] Entities in DLC arrangements reporting under Chapter 2M must prepare financial statements in accordance with Australian accounting standards and other financial reporting requirements of the Corporations Act (“Australian GAAP”). ASIC expects combined financial statements to be prepared in accordance with Australian GAAP. ASIC would not envisage granting relief to allow the Australian entity to report in accordance with a foreign GAAP.

[Historical note: PN 71.15 replaced 7/5/2003. The paragraph formerly read:

“[PN 71.15] ASIC would not envisage granting relief from any requirements for entities reporting under Chapter 2M to:

- (a) prepare, lodge, distribute and present consolidated financial statements and single entity financial statements for any Australian entity.*
- (b) prepare the financial statements in Australian dollars. ASIC would expect that the combined financial statements be prepared in Australian dollars, in accordance with the usual requirements of the Corporations Act 2001. ASIC may consider relief to include information in other currencies in additional columns.*
- (c) prepare financial statements in accordance with Australian accounting standards and other financial reporting requirements of the Corporations Act 2001. ASIC would expect combined financial statements to be prepared in accordance with Australian accounting standards and the other usual financial reporting requirements of the Corporations Act 2001 (“Australian GAAP”).”.]*

[PN 71.16] However, in the combined financial statements, a particular item or matter included in the consolidated financial information relating to the listed foreign company and its controlled entities could be accounted for in accordance with accounting standards of the listed foreign company's place of origin ("the foreign GAAP") instead of the requirements of an Australian GAAP where:

- (a) for the particular item or matter, the application of Australian GAAP is so anomalous that it clearly would not give a true and fair view in the combined financial statements (eg because the combined financial statements will not show the profits available for the listed foreign company to pay dividends);
- (b) the treatment of the item or matter under the foreign GAAP differs very materially from the treatment under Australian GAAP;
- (c) applying the foreign GAAP in the combined financial statements to an item or matter included in the listed foreign company's consolidated financial information would not affect the ability of either the listed foreign company or the listed Australian company as single entities to pay the same level of dividends as would have been the case in the absence of applying the foreign GAAP; and
- (d) A note to the combined financial statements shows the effect had those combined financial statements been prepared fully in accordance with Australian GAAP.

[PN 71.16A] Given the unique nature of DLC arrangements that involve listed companies in two different jurisdictions, ASIC will consider applications from the Australian listed entity for any of the following types of case-by-case relief:

- (a) Relief from the requirements to prepare, lodge and distribute consolidated financial statements.
- (b) Relief from the requirement to distribute single entity financial statements for the listed Australian entity. Conditions of relief would include providing certain summarised single entity financial information in the full financial report, and making the full single entity financial statements available on the entity's website, and to members free of charge on request (including a standing request).
- (c) Relief to disclose information in a foreign currency in addition to Australian dollars. ASIC will also consider applications for relief to prepare the financial statements in the currency of a major jurisdiction instead of in Australian dollars. The foreign currency would need to be a major currency for international transactions and be the "functional currency" of the combined group as a whole for the purposes of International Accounting Standards Board's exposure draft of an improved IAS 21. The combined group would need to operate globally, have a large portion of its operations offshore, and a substantial proportion of its combined shareholders would not be Australian residents.

It must be reasonable to expect that international analysts in the industry in which the combined group mainly operates would predominantly focus on financial information in the chosen foreign currency.

Any applications should be prepared with regard to the requirements of s340 and 342 of the *Corporations Act 2001*, as well as Policy Statement 43 *Accounts and audit relief* [PS 43] and Policy Statement 51 *Applications for relief* [PS 51].

[Historical note: PN 71.16A inserted 7/5/2003.]

Information reported overseas

[PN 71.17] The Australian entity in a DLC structure must distribute or make available single entity, consolidated and, where applicable, combined information to all of its members in the manner described in s314– 316 of the *Corporations Act*. The full financial report would include the full single entity information, full consolidated information and, where applicable, full combined information. Any concise financial report would include concise consolidated information and, where applicable, concise combined information, but need not include single entity information. As stated above, this information would be in accordance with Australian reporting requirements and be presented in Australian dollars.

[PN 71.18] In addition, the full financial report and concise financial report should contain a prominent note stating that members of the Australian entity may request that any financial report or other financial statement information (including a reconciliation to foreign GAAP) lodged or distributed in another jurisdiction by either of the two listed entities in the DLC structure (eg a US Form 20F) be sent to them at no charge.

That annual information should be presented in English and should be lodged with the ASX on the next business day after it is disclosed in the other country (see also s323DA of the *Corporations Act* and, for an exempt foreign entity listed in Australia, rule 1.15.2 of the ASX Listing Rules). The information should also be made freely available on the company's internet site no later than the next business day after being lodged with the ASX.

[PN 71.19] The information detailed in [PN 71.18] should be sent to members who request that information by the later of:

- (a) 7 days after the request is made; and
- (b) 7 days after the information is first lodged with the ASX.

[PN 71.20] Half-year financial statement information lodged or distributed by either of the DLC companies in countries other than Australia should also be lodged with the ASX (see also s323DA of the Corporations Act and, for an exempt foreign entity listed in Australia, rule 1.15.2 of the ASX Listing Rules). The Australian entity should make this information available on its internet site if the entity's own half-year financial report is made available either on its own internet site or on the internet site of the other listed entity in the DLC structure. The information should be made freely available no later than the next business day after being lodged with the ASX.

[PN 71.21] Having regard to the requirements of para 4.6 of AASB 1018 "Statement of Financial Performance" and s295(2) of the Corporations Act, the financial report of the Australian entity in a DLC structure must only include financial statements prepared in accordance with Australian GAAP and may not include financial statements prepared in accordance with foreign GAAP. Some information may be included in accordance with foreign accounting standards (eg a GAAP reconciliation) provided that it is not in the form of financial statements and is not given undue prominence relative to the information prepared in accordance with Australian GAAP.

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Features of DLC structures considered by ASIC

1. DLC structures are formed by way of agreements between two entities and amendments to their constitutions. The arrangement does not involve any agreements between shareholders but the shareholders of each company will approve DLC arrangements between the companies and the changes to the constitutions of the companies.
2. The key features of the DLC structures put to ASIC are:
 - (a) Each company retains its legal identity and, except for transfers necessary for dividend equalisation purposes, assets and businesses are only transferred between the two companies for fair values.

- (b) The votes of the shareholders of one company are taken into account for resolutions of the second company through a mechanism involving the use of special purpose entities, except for certain matters involving “class rights”. The effect is that the shareholder groups of the companies vote on resolutions of both companies as if they were a single group. The votes exercisable by each group of shareholders are in proportion to an “Equalisation Ratio” that is determined on a basis agreed at the commencement of the DLC arrangements. Subsequent to commencement of the DLC arrangements, the Equalisation Ratio may be adjusted for the effects of share capital changes for either entity (eg certain new issues or buy-backs).
- (c) There is no change in the respective shareholders of each company as a result of entering into the DLC arrangement, although there is a sharing of rights between the shareholders’ groups.
- (d) The companies have separate boards appointed at separate general meetings, but these boards have common directors.
- (e) The entities seek to declare equalised dividends and other distributions, on the basis of the Equalisation Ratio.
- (f) There are arrangements for equalisation payments between the two companies to enable a company that is unable to pay a dividend to do so.
- (g) The shareholders of each company retain the right to terminate the DLC structure at any time without any significant penalty at a meeting at which the shareholders of the other company have no voting rights on any resolution to effect such a termination, subject to such termination also being separately agreed by the shareholders of the other company in a similar manner at a meeting of the other company.
- (h) The two companies may enter into deeds of cross guarantee.
- (i) The constitutions of the companies allow shareholders of the two companies to participate on winding up of both companies by reference to Equalisation Ratio.