



Grant Thornton



LETTER OF COMMENT NO. 10

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RE: File Reference No. 1500-100R

Grant Thornton LLP appreciates the opportunity to respond to the Request Related to the October 2006 FASB Exposure Draft, *Not-for-Profit Organizations: Mergers and Acquisitions*. We support the Board's tentative decision to address a merger of not-for-profit organizations as a transaction distinct from an acquisition.

With limited additional guidance described below, we believe that the Board's tentative definition of a merger of two or more not-for-profit organizations would appropriately distinguish between a merger and either an acquisition or the formation of a joint venture. As described in our responses to the questions posed in the request for comments, we suggest that the FASB

- Not provide a detailed list of factors or rules to distinguish a merger from either an acquisition or the formation of a joint venture
- Emphasize that the change of control over a merging organization must be substantive and not temporary
- Provide a few examples to illustrate the application of the merger definition
- Consider whether the definition of a joint venture should be clarified for not-for-profit ventures

Questions posed by the request for comments

Question 1: *Is the definition of a merger appropriate for distinguishing mergers from acquisitions by not-for-profit organizations? If not, why?*

Yes, we believe that the Board's tentative definition of a merger of two or more not-for-profit organizations would appropriately distinguish between acquisition and merger transactions.

Question 2: *Would the definition of a merger, together with the definition of control, be workable in practice? That is, can it be applied in practice with a reasonable degree of*

consistency, particularly in distinguishing a merger from the transactions noted in paragraph 6(a) and 6(b)? If not, why, and how might it be improved?

Distinguishing a merger from an acquisition (paragraphs 6(a) and 11)

We believe that the Board's tentative definition of a merger would provide a reasonable and principled approach to distinguishing a merger from an acquisition. The application of the definitions would require consideration of all relevant facts and circumstances of a particular situation to determine if and when an actual change of control has occurred. However, we think that the Board should not provide detailed guidance or rules to specify which changes in organizational governance and structure would represent a change of control.

Paragraph 6(a) of the request for comments describes a transaction as follows: "an acquisition in which one entity acquires another entity by gift (that is, the acquired entity donates its net assets to the acquiring entity)." Paragraph 11 appears to describe the Board's concerns about the ability to appropriately identify such a transaction using the tentative definition of a merger, as follows:

[An] organization may attempt to disguise an acquisition as a merger. For example, if one organization's governing body donates the net assets of the organization to another organization, the parties to the merger may attempt to structure the Board composition of the acquiring organization to make it appear as if the acquisition was a merger.

With respect to the transactions described in paragraphs 6(a) and 11, judgment would be required to determine whether a receiving organization had effectively gained control of a gift or had ceded control of its own precombination activities. Although we do not support providing detailed guidance or rules to specify which changes in organizational governance and structure would represent change of control, we suggest that the FASB consider providing an example, such as that in paragraph 11, to illustrate the application of the definition.

Distinguishing a merger from the formation of a joint venture

Paragraph 6(b) describes a transaction as follows:

A 'combination' that is in substance a joint venture in which the net assets of two nonprofit activities are joined together for a period of time with an expectation or possibility that the activities would revert back to the venture partners in the future.

To address the concerns raised in paragraph 6(b), the FASB could emphasize that in a merger transaction, the change of control over the merging organizations must be substantive and not temporary. We note that the definition of a *corporate joint venture* in APB Opinion 18, *The Equity Method of Accounting for Investments in Common Stock*, does not require that the venture be of limited duration. However, the determination of whether a transaction is a merger or the formation of a joint venture would be based on all relevant facts and circumstances rather than on one isolated factor.

Question 3: Do the definitions of a merger and control, taken together, make it sufficiently clear that transferring an integrated set of net assets to a newly created joint venture in which the transferor retains shared control is not the equivalent of ceding control? If not, how might the Board clarify the definitions or make it clear that the creation of a joint venture is beyond the scope of the proposal?

We think that the Board members' concerns about ability to distinguish a merger from the formation of a joint venture may indicate that the definition of a joint venture or its application to not-for-profit ventures lacks clarity.

Shared control

Questions 3 and 4 and paragraph 10(a) of the request for additional comments all seem to presume that the existence of shared control by itself is sufficient to define a joint venture and to distinguish its formation from a merger transaction. We believe that such a presumption would be inappropriate. A merger is likely to involve shared control rather than the unilateral control of an acquirer, and therefore a merger with shared control might be distinguished from a joint venture by other characteristics, such as expected duration and the existence or absence of opt-out clauses. We note that in EITF Issue 98-4, "Accounting by a Joint Venture for a Business Received at its Formation," the SEC Observer indicated that the staff would object to a conclusion that joint control is the only defining characteristic of a joint venture.

Question 4: Does the definition of a merger require any additional criteria or guidance to address the concern noted in paragraph 10? That is, in general, will the ceding of control be discernable in practice from the surrounding facts and circumstances, despite the possibility that some entities may attempt to structure the new organization's Board composition, senior management, or charter to disguise circumstances in which one of the governing bodies retains control over the newly created organization?

Please see our responses to Questions 3 and 5.

Question 5: If one or more parties to a potential combination retains an opt-out clause, would that alone be sufficient evidence to determine that that party has not ceded control? Some respondents asked the Board to consider whether retention of so-called opt-out clauses by the parties to a combination would indicate that a merger or acquisition had not occurred. The staff has been told that such contingent provisions sometimes are included in acquisitions of physician practices by not-for-profit organizations. However, presumably, such provisions could occur in mergers or acquisitions of other private practices, including acquisitions by business entities. The staff thinks that the specific terms of each contractual arrangement need to be assessed to determine whether the definition of a merger or acquisition has been met and would not expect a unique interpretation for mergers or acquisitions by not-for-profit organizations.

"Opt-out" clauses are not unique to not-for-profit organization mergers and acquisitions and are not specifically addressed in FASB Statement 141 (revised 2007), *Business Combinations*.



We think that the Board should not provide a unique interpretation for mergers or acquisitions by not-for-profit organizations.

We would be pleased to discuss our comments with Board members or the FASB staff. If you have any questions, please contact Ann McIntosh at 612.677.5257.

Very truly yours,

/s/ Grant Thornton LLP