Heads Up

Audit and Enterprise Risk Services

December 12, 2007
Vol. 14, Issue 26

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To Merge and Converge

Major Changes to Business Combination Accounting as FASB and IASB Substantially Converge Standards

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Introduction

Statements 141 and 142,[1] issued back in 2001, marked just the first phase of a multiphase project to reconsider the accounting for business combinations. That effort not only eliminated the pooling of interest method of accounting and the amortization of goodwill, but also carried forward without reconsideration much of the already established guidance on purchase accounting (now referred to as the "acquisition method").

The FASB recently completed the second phase of this project, to date the most significant convergence effort with the IASB,[2] and on December 4, 2007, issued the following two accounting standards:

- Statement No. 141(R), *Business Combinations*.
- Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements* — an amendment of ARB No. 51.

These statements substantially elevate the role played by fair value and dramatically change the way companies account for business combinations and noncontrolling interests (*minority interests* in current GAAP). Compared with their predecessors, Statements 141(R) and 160 will require:

- More assets acquired and liabilities assumed to be measured at fair value as of the acquisition date.
- Liabilities related to contingent consideration to be remeasured at fair value in each subsequent reporting period.
- An acquirer to expense acquisition-related costs (e.g., deal fees for attorneys, accountants, investment bankers).
- Noncontrolling interests in subsidiaries initially to be measured at fair value and classified as a separate component of equity.

[1] For the full titles of the standards, see Appendix F.
[2] Because the IASB has not yet issued its final statements, this *Heads Up* reflects the IASB's decisions to date. The IASB expects to issue IFRS 3 (revised) and IAS 27 (revised) in early 2008.

Editor's Note: Upon the adoption of Statement 141(R), all assets acquired and liabilities assumed in a business combination (other than those described in Appendix A, Question 14) must be measured at fair value in accordance with Statement 157 (see also Deloitte & Touche LLP's September 27, 2006, *Heads Up*).[3] Previously, entities that had already adopted Statement 157 could apply a practicability exception for certain assets acquired and liabilities assumed in a business combination that are measured under Statement 141 on a basis that is inconsistent with Statement 157's definition of fair value.

The Urge to Converge

The primary motive of the FASB and IASB in undertaking this project was to converge their guidance on accounting for business combinations and noncontrolling interests; however, this convergence was not a complete success. Ultimately, the two boards were unable to reach mutual conclusions in several key areas, including the following:

- The IASB allows entities to record, on a transaction-by-transaction basis, noncontrolling interests at **either** fair value (in a manner consistent with Statement 141(R)) **or** at the acquiree's proportionate share of the fair value of the net identifiable assets (i.e., no goodwill is recorded for the noncontrolling interests). The latter represents the current accounting under IFRS 3.
- Under IFRS 3 (revised), the acquirer recognizes a contingent liability assumed in a business combination if it is a present obligation that arises from past events and its fair value can be measured reliably. In contrast, Statement 141(R) establishes a recognition threshold for noncontractual contingencies (i.e., whether it is more likely than not that such a contingency meets the definition of an asset or liability).
- Statements 141(R) and 160 are effective for fiscal years beginning on or after December 15, 2008, while IFRS 3 (revised) and IAS 27 (revised) are effective for annual periods beginning on or after July 1, 2009.
- The IASB permits early adoption while the FASB does not.

For a comprehensive list of differences between the FASB and IASB standards, see Appendix E.

The FASB has not only given a generous amount of time in which to implement both statements, but it has also provided for prospective application in fiscal years beginning on or after December 15, 2008.

Effective Date and Transition

Good news for preparers! The FASB has not only given a generous amount of time in which to implement both statements, but it has also provided for **prospective** application in fiscal years beginning on or after December 15, 2008. That means Statement 141(R) applies only to business combinations **consummated** after that date (with one important exception for income taxes — see Editor's Note on next page). However, Statement 160 requires entities to apply its presentation and disclosure requirements retrospectively (e.g., by reclassifying noncontrolling interests to appear in equity) in comparative financial statements, if presented (see Appendix B, Question 4, for a complete list of items that require retrospective application). In addition, both statements prohibit earlier application of the guidance.

[3] The FASB recently decided to defer the effective date of Statement 157 for nonfinancial assets and liabilities by one year (i.e., until fiscal years beginning after November 15, 2008). The deferral will be effective upon the issuance of a final FASB Staff Position.

Editor's Note: Although the transition provisions of Statement 141(R) appear to affect only business combinations consummated after its effective date, this is not entirely the case. Under current GAAP, any changes in an acquired entity's deferred tax assets and uncertain tax position balances (except for changes in valuation allowances for acquired deferred tax assets) are generally recorded through goodwill, regardless of whether such changes occur during the *allocation period* (see Appendix A, Question 30) or thereafter. On the other hand, Statement 141(R) requires that any adjustments to an acquired entity's deferred tax assets and uncertain tax position balances that occur after the *measurement period* (see Appendix A, Question 30) be recorded as a component of income tax expense. Under the transition provisions of Statement 141(R), the new requirement applies to all business combinations, regardless of the consummation date.

In other words, this requirement is the one transition provision that could affect future accounting for business combinations consummated before Statement 141(R)'s effective date (see Example 2 in Appendix A, Question 2).

More Assets and Liabilities at Fair Value

Statements 141(R) and 160 continue the FASB's push toward more fair value in financial statements. Underlying Statement 141(R) is the fundamental principle that an acquirer should measure all assets acquired and liabilities assumed at fair value as of the acquisition date.[4] Below is a partial list of certain assets and liabilities that generally will be accounted for differently under Statement 141(R) (see Appendix C for a more comprehensive list of changes from current practice):

Statements 141(R) and 160 continue the FASB's push toward more fair value in financial statements.

Item	Statement 141(R)	Statement 141
Contingent consideration — commonly referred to as an "earnout" (see Appendix A, Questions 8 and 9)	Include, in the acquisition accounting, at fair value (either as a liability or in equity, depending on its nature). For contingent consideration recorded as a liability, subsequent changes in fair value are recognized in the income statement (until settled). Contingent consideration recorded as equity is not subsequently remeasured.	Generally, record as an adjustment in the postcombination period when the contingency is resolved and the consideration is issuable. An amount is often not recognized as of the acquisition date, nor does resolution of the contingency result in an income statement impact.
Restructuring costs — e.g., anticipated costs of exiting an activity/ business of the acquired entity, involuntary severance, relocation of an acquiree's employees (see Appendix A, Question 18)	Only restructuring costs of the acquiree that meet the recognition criteria in Statement 146 as of the acquisition date are included in the fair value allocation. All others are postcombination costs that are recognized in the income statement when incurred. Most restructuring reserves recognized under Statement 141 cannot be recognized under Statement 141(R).	Restructuring costs are recognized as a liability in the purchase price allocation provided that certain conditions in Issue 95-3 are met.

4 See Editor's Note on page 5.

Item	Statement 141(R)	Statement 141
In-process research and development (IPR&D) — an acquired intangible asset related to research and development activities of the acquiree (see Appendix A, Question 20)	Under Statement 142, as amended by Statement 141(R), acquired IPR&D is capitalized as an indefinite-lived intangible asset until completion or abandonment of the project. Upon completion, the research and development asset is accounted for as a finite-lived intangible asset and amortized over the related product's estimated useful life. If the project is abandoned, the asset is expensed immediately if no alternative future use exists.	The fair value of IPR&D with no alternative future use is charged to expense as of the acquisition date.
Preacquisition contingencies — e.g., a preexisting lawsuit of the acquired entity (see Appendix A, Question 24)	Contractual contingencies, and those noncontractual contingencies that more likely than not meet the definition of an asset or liability, are recognized at fair value as of the acquisition date. In subsequent periods, (1) a contingent asset is remeasured to the lower of its acquisition-date fair value or the best estimate of its future settlement amount and (2) a contingent liability is remeasured to the higher of its acquisition-date fair value or the amount that would be recognized under Statement 5. Subsequent changes in measurement are included in income.	Recognize at fair value, if determinable, during the allocation period. Otherwise, follow Statement 5 and recognize, if probable and the amount is reasonably estimable, during the allocation period. Often, no amount is recorded as of the acquisition date. Therefore, the impact of the settlement of a contingency is typically recorded in the postcombination income statement.
Bargain purchase — previously referred to as negative goodwill (see Appendix A, Questions 28 and 29)	Recognize a gain in the period the acquisition occurs. The gain is calculated as the excess of the fair value of the net assets acquired over the sum of (1) the fair value of the consideration transferred, (2) the fair value of any previously held equity interests, and (3) the fair value of any noncontrolling interests. There is no pro rata reduction of certain noncurrent assets.	The excess of the fair value of the net assets acquired over the fair value of the consideration transferred reduces certain noncurrent assets on a pro rata basis. Any amount of the excess that remains after these assets are reduced to zero is recognized as an **extraordinary** gain.

Editor's Note: Not every asset acquired or liability assumed is measured at fair value under Statement 141(R). For example, deferred taxes, employee benefits, and share-based payments continue to be measured in accordance with other applicable accounting literature. In fact, Statement 141(R) introduces several new exceptions to the fair value measurement principle (see Appendix A, Question 14). Nonetheless, Statement 141(R)'s substantial expansion of acquisition-date and subsequent-period fair value measurements, including fair-value-based impairment tests for intangible assets not previously recognized (e.g., assets an acquirer does not intend to use), will require valuation professionals to be more involved in preparing and auditing financial statements.

Other Significant Provisions of Statement 141(R)

Statement 141(R) makes other significant changes to current practice, some necessitated by the FASB's fundamental principle that assets acquired and liabilities assumed be recognized at fair value as of the acquisition date. In particular, Statement 141(R) requires the following:

Statement 141(R)'s fair value measurements will require valuation professionals to be more involved in auditing and preparing financial statements.

Measurement Date of Acquirer's Equity Securities Issued — Statement 141(R) requires that equity securities issued as consideration in a business combination be recorded at fair value as of the acquisition date (see Appendix A, Question 4, for more guidance on determining the acquisition date). Currently, under Issue 99-12, the acquirer's equity securities are valued over the period a few days before and after the terms of the business combination are agreed to and announced. Because the value of securities often changes dramatically between the announcement date and acquisition date, the new rules might result in substantially different amounts recorded as consideration (see Appendix A, Question 6).

Measurement Period — Statement 141(R) retains its predecessor's *allocation period* (referred to in Statement 141(R) as the *measurement period*), in which up to one year is given to complete the business combination accounting. During the measurement period, beginning after the consummation of a business combination, the acquirer gathers information necessary to complete the acquisition accounting (e.g., to complete the valuation of certain assets and liabilities). Any adjustments must relate to facts and circumstances that existed as of the acquisition date. Contrary to prevailing practice, in which any adjustments to provisional amounts recorded during the allocation period are generally accounted for prospectively, Statement 141(R) requires an acquirer to **revise** comparative information for prior periods presented (see Appendix A, Questions 30 and 31).

Transaction Costs — Direct and incremental costs incurred in the business combination (e.g., deal fees for legal, accounting, investment banking) must be expensed as incurred, bringing to an end the current requirement of capitalizing these costs as part of the acquisition. Expensing transaction costs is consistent with Statement 157, which generally concludes that transaction costs are not a component of the fair value of an asset acquired (see Appendix A, Question 7).

Leveraged Recapitalizations and Buyouts — While Statement 141(R) will not affect the accounting for leveraged recapitalizations, it will nullify Issue 88-16, eliminating the complex accounting for leveraged buyouts (see Appendix A, Question 35).

Noncontrolling Interests of a Subsidiary

In accordance with Statements 141(R) and 160, when a parent company acquires control of a subsidiary, it must include **100 percent** of the fair value of all the acquired company's assets and liabilities in its consolidated financial statements[5] — regardless of whether the new parent buys greater than 50 percent, 100 percent, or any percentage

[5] See Editor's Note above.

in between, of the target. The acquirer must recognize the noncontrolling interest at fair value and allocate goodwill between the controlling and noncontrolling interest holders. The FASB based its decision on the premise that a change of control is a significant economic event whereby an acquirer gains control of a target. Put another way, by virtue of its majority interest, the acquirer controls **all** of the assets acquired and liabilities assumed, regardless of the percentage of the equity interest held by the minority.

Example

Company X obtains control of Company Y by acquiring 51 percent of Y's equity. Before the purchase, X held no equity in Y. Because it now controls Y, X includes 100 percent of Y's assets and liabilities in its consolidated financial statements at their fair value as of the acquisition date. In comparison, current GAAP require X to recognize each asset and liability (those that must be measured at fair value as of the acquisition date) as a mixture of current fair value (51 percent) and Y's carryover basis (49 percent).

Some financial statement users believe that current GAAP, by mixing older costs and current fair values in the reported amount of a single asset or liability, make financial statements less understandable and less useful, and prevent them from faithfully representing the realities of the acquisition. While the statements certainly do not solve all perceived problems with a mixed-attribute model (combining historical costs and fair values within a single set of financial statements), some critics of the current model view the development as a step in the right direction.

Implementation issues will most likely surface over the next year as entities begin to consider how the new rules affect their pending acquisitions.

Financial analysts: take note. **Under Statement 160, noncontrolling interests in a subsidiary,** currently recorded within "mezzanine" (or temporary) equity or as a liability, **will be included in the equity section of the balance sheet.** Therefore, shareholders' equity will increase by the fair value of the noncontrolling interest simply by virtue of a partial acquisition. When an acquirer obtains control of another entity, any equity interests previously held are remeasured at fair value (with any gain or loss recognized in the income statement); any subsequent increase or decrease in the equity interests of that subsidiary held by the parent (provided that control is retained) is recorded as an equity transaction. This means that step acquisition accounting, as well as gains and losses (e.g., SAB 51) on dispositions of equity interests, when control is retained, will be a thing of the past.

Example

On January 15, 2009, Company X obtains control of Company Y by acquiring 51 percent of Company Y's equity interests. (Because it now controls the target, under Statement 141(R), X includes 100 percent of Y's assets and liabilities in its consolidated financial statements at their fair value as of the acquisition date.) On June 15, 2009, X acquires an additional 20 percent interest in what is now Subsidiary Y. Then, on September 30, 2009, X sells 20 percent of its holdings for a significant premium (returning to 51 percent ownership). Since X had control of Subsidiary Y before the new acquisition and retains control after the disposition, these transactions — including any "gain" or "loss" — are recorded as equity transactions (see Appendix B, Question 7).

Final Thoughts

The statements will garner much publicity and perhaps their share of criticism. In addition, because of their sheer volume (together, the statements contain more than 400 pages of guidance) and the inherent complexities in applying their provisions, implementation issues will most likely surface over the next year as entities begin to consider how the new rules affect their pending acquisitions.

On December 17, 2007, we will host a *Dbriefs* webcast on Statements 141(R) and 160. Register for this webcast for an in-depth analysis of these statements. Also, in 2008, look for the second, updated edition of our Roadmap series publication, *Accounting for Business Combinations, Goodwill, and Other Intangible Assets — A Roadmap to Applying Statements 141 and 142*.

Appendix A (Statement 141(R)) and Appendix B (Statement 160) of this *Heads Up* discuss, in question-and-answer format, details of many of the issues described above, as well as a host of other topics.

Appendix C offers an at-a-glance comparison of the key differences between Statements 141(R) and 160 and current GAAP.

Appendix D summarizes key changes that the FASB made to the June 2005 Exposure Drafts in finalizing Statements 141(R) and 160.

Appendix E offers an at-a-glance comparison of the key differences between the statements and the revised IFRSs to be issued in 2008.

Appendix A

Q&As Related to Statement 141(R) (Business Combinations)

Click a question below to jump to its related Q&A.

Scope

Effective Date and Transition

Identifying the Acquirer

The Acquisition Date

Measuring the Fair Value of the Acquiree

Consideration Transferred

Assets Acquired and Liabilities Assumed

* The FASB's redeliberations of the Exposure Draft that preceded Statement 141(R) did not result in many changes to the provisions included in the final statement. Therefore, questions marked with an "*" have been carried forward generally unchanged from Deloitte & Touche LLP's June 30, 2005, *Heads Up*.

17. Is an acquirer required to recognize assets that it does not intend to use or use in a way other than their highest and best use? If so, how should those assets be valued?
18. Can an acquirer recognize a liability for restructuring costs related to the acquiree that it expects to incur as part of the business combination?
19. Does Statement 141(R) provide any guidance on the recognition, measurement, and subsequent accounting for reacquired rights?
20. What is acquired in-process research and development (IPR&D), and how is it accounted for under Statement 141(R)?
21. If control is obtained, but less than 100 percent of a business is acquired, how does Statement 141(R) change the determination of the amounts assigned to identifiable assets acquired and liabilities assumed?*
22. How are noncontrolling interests in an acquired business measured in the fair value allocation?
23. Does Statement 141(R) change how intangible assets are recognized apart from goodwill?
24. How are contingent assets acquired and contingent liabilities assumed accounted for under Statement 141(R)?

Assessing What Is Part of the Exchange for the Acquiree

25. Does Statement 141(R) clarify which parts of the transaction price (or other payments made by the acquirer) should be included in the business combination accounting and which should not?

Goodwill

26. Does the definition of goodwill change under Statement 141(R)?*
27. How is goodwill allocated to the controlling interest and noncontrolling interests?

Bargain Purchases

28. What is a bargain purchase?
29. How is a bargain purchase accounted for?

Measurement Period

30. What is a measurement period?*
31. If, during the measurement period, an adjustment is made to the provisional amounts assigned to identifiable assets acquired and liabilities assumed (as contemplated in the previous question), how is that adjustment reported?

Income Taxes

32. Does Statement 141(R) provide guidance on changes in the acquired entity's deferred tax asset and uncertain tax position balances subsequent to the business combination?

Other

33. How are reverse acquisitions accounted for?*
34. How does the parent company account for acquisitions of noncontrolling interests?*
35. Does Statement 141(R) affect the accounting for leveraged buyouts (LBOs) and leveraged recapitalizations?

Scope

1. What transactions are within the scope of Statement 141(R)?

Once effective, Statement 141(R) will apply whenever an acquirer obtains control of one or more **businesses.** Regarding the determination of whether the assets acquired and liabilities assumed constitute a business, Statement 141(R) nullifies Issue 98-3 and incorporates the definition of a business included therein, with some important modifications. For example, to qualify as a business under Statement 141(R), an entity no longer has to be "self-sustaining," and a group of assets no longer needs to have outputs. That is, development-stage entities could now be businesses under Statement 141(R). As a result, some transactions that are considered asset acquisitions under current GAAP will be business combinations under Statement 141(R).

Statement 141(R) also applies to combinations between mutual enterprises (e.g., cooperatives, credit unions), for which Statement 141 temporarily deferred application of the purchase method of accounting. In addition, Statement 141(R) applies to situations in which control of a business is obtained without the transfer of assets (e.g., if the acquiree repurchases enough of its own shares to give an existing investor control).

In a manner consistent with current GAAP, Statement 141(R) excludes from its scope formations of joint ventures, acquisitions of assets or asset groups that do not constitute a business, combinations of entities or businesses under common control, and acquisitions by not-for-profit organizations of businesses and other not-for-profit organizations. However, the FASB issued an Exposure Draft in October 2006 that proposes new guidance for not-for-profit organizations, and intends to address joint venture issues in a future project.

Effective Date and Transition

2. What are the effective date and transition provisions of Statement 141(R)?

Statement 141(R) requires *prospective* application for business combinations consummated in fiscal years beginning on or after December 15, 2008, except as discussed below for income taxes. Early application is prohibited. The effective date of the replacement of IFRS 3 is for annual periods beginning on or after July 1, 2009, and the IASB is allowing early adoption. Assets acquired and liabilities assumed in business combinations whose acquisition dates precede the effective date of Statement 141(R) should not be adjusted upon adoption.

Example 1

On December 1, 2008, Company A acquires 100 percent of Company B. As part of the transaction, A has provided the selling shareholders with an earnout that will pay them a specified amount of cash; payment of this earnout is contingent upon achieving certain earnings targets. Partly because the selling shareholders will not provide future services to A, management determined that the arrangement did not represent compensation expense. Because the business combination is consummated before the effective date of Statement 141(R), A would not be permitted to record the contingent consideration at fair value upon the adoption of Statement 141(R). Therefore, A would continue to follow the guidance in paragraphs 25–28 of Statement 141.

One area in which Statement 141(R)'s transition provisions may affect transactions consummated before its effective date is income taxes. Statement 141(R) nullifies Issue 93-7, which generally required entities to record adjustments to deferred tax assets (except for changes in valuation allowances for acquired deferred tax assets) and uncertain tax position balances arising in a business combination as an increase or decrease to goodwill (irrespective of whether this adjustment occurs within the one-year allocation period). Under the transition provisions of Statement 141(R), the new requirement applies to all business combinations, regardless of the consummation date (see Question 32). In other words, this requirement is the one transition provision that could affect future accounting for business combinations consummated before Statement 141(R)'s effective date.

Example 2

On January 15, 2005, Company X acquired 100 percent of Company Y. As part of the purchase accounting, X recognized a liability associated with an uncertain tax position. On December 31, 2006, X increased the liability to reflect a change in its best estimate of the ultimate settlement with the taxing authority. In accordance with Issue 93-7, X recorded this adjustment as an increase to goodwill. After the adoption of Statement 141(R), X will be required to record any additional adjustments to the liability as a component of income tax expense.

Identifying the Acquirer

3. Does Statement 141(R) change the requirements under Statement 141 for identifying the acquirer?

Statement 141(R) carries forward the same criteria in Statement 141 for identifying the acquirer, but does make one amendment to Interpretation 46(R). The amendment requires that if the entity acquired (1) is a variable interest entity (VIE) and (2) meets the definition of a business in Statement 141(R) (see Question 1), then the VIE's primary beneficiary is the acquirer and must apply Statement 141(R).

The Acquisition Date

4. As of what date should the business combination be recorded?

In a manner consistent with current GAAP, the business combination should be recorded as of the date on which the acquirer obtains control of the acquiree, generally referred to as the "acquisition date."

The acquisition date is important because on this date:

- The fair value of the acquired business is measured.
- The fair value of the acquirer's equity securities issued to the seller is measured (see Question 6).
- The fair value of the assets acquired, liabilities assumed, and noncontrolling interests is measured.
- The acquirer begins consolidating the acquired entity's financial position, results of operations, and cash flows.

Under Statement 141, the acquirer may, for convenience, designate the end of an accounting period between the initiation date and consummation date of a business combination as the effective date (commonly referred to as the "convenience date"). Statement 141(R) eliminates the notion of a convenience date.

Measuring the Fair Value of the Acquiree

5. Can the fair value of an acquiree be extapolated from the consideration transferred when less than 100 percent is acquired?

Not necessarily. Although sometimes 100 percent of the fair value of the acquiree may be determined by multiplying the price paid per share by the number of the acquiree's outstanding shares, acquirers should not automatically assume this. For example, if 80 percent of an entity is acquired for $80, 100 percent of the acquiree's fair value may not necessarily be $100.

Why would the amounts differ? One explanation is evidence of a control premium, which would result in more value associated with the controlling interest than with the noncontrolling interest.

Example

Assume that a company announces it will acquire 60 percent (600,000 shares) of an entity for $6 million (or $10 per share). However, as of the date the terms of the acquisition are agreed to (and as of the acquisition date), the acquired entity's shares are trading at $7.50 per share. The acquirer acknowledges that a premium over market is paid because of synergies it believes it will gain. Therefore, it may not be reasonable to conclude that the fair value of the entire acquired entity is $10 million. Instead, the fair value of the acquired entity might be $9 million, calculated as the $6 million paid plus $3 million for the noncontrolling shares (400,000 shares × $7.50 per share).

Preparers will need to determine whether an extrapolation of the consideration paid appropriately reflects the fair value or whether other methods should be used to estimate fair value. If a quoted market price is not available, the best support for management's estimate of fair value would be a contemporaneous valuation performed using an appropriate valuation method (generally, under the market or income approaches described in Statement 157). For many acquisitions of less than 100 percent of an entity (especially those involving nonpublic entities), separate valuations will be sought because the cost of the interests obtained cannot be appropriately extrapolated to the value of the unacquired interests. Estimation of the fair value of the noncontrolling interest of the acquired entity will be important since it will affect the amount of goodwill attributable to the noncontrolling interest.

Consideration Transferred

6. When an acquirer's equity securities are issued to the seller as consideration for the acquired business, as of what date are those equity securities valued?

Under Statement 141(R), equity securities are measured as of the acquisition date and are included in the fair value of the consideration transferred to the seller. Under current GAAP, the acquirer's equity securities transferred to the seller are generally measured on the basis of the share prices over the period a few days before and after the terms of the combination are agreed upon and announced. Therefore, the consensus in Issue 99-12 is nullified. This provision of Statement 141(R) could significantly change the value recorded for the acquired business if share prices differ between the date the terms of the combination are agreed upon and announced and the acquisition date.

7. How should the acquirer's direct and incremental costs of the acquisition be accounted for?

Direct and incremental costs incurred as a result of the business combination (e.g., deal fees for legal, accounting, investment banking) must be expensed as incurred, a significant change from current GAAP. Costs incurred for the issuance of debt or equity securities to effect the combination are not within the scope of Statement 141(R) and would be accounted for in accordance with other applicable GAAP.

Statement 141(R) also stipulates that an agreement by the acquirer to reimburse the acquiree or its former owners for paying the acquirer's acquisition-related costs is a separate transaction from the business combination. In other words, these costs must be expensed and excluded from acquisition method accounting.

8. What is contingent consideration and how is it accounted for as of the acquisition date?

Contingent consideration represents obligations of the acquirer to transfer additional assets (e.g., cash) or equity interests to the former owners of the acquired entity if specified future events occur or conditions are met.

An important change in Statement 141(R) is that the fair value of all contingent consideration is recorded in the financial statements as of the acquisition date. Depending on the nature of the contingent consideration (i.e., liability or equity), it may be remeasured to fair value at the end of each reporting period until its settlement. For more details, see Question 9.

9. How will contingent consideration be accounted for after the acquisition date?

Although the fair value of all contingent consideration is included as part of the consideration transferred as of the acquisition date, only contingent consideration that is classified as a liability is remeasured to fair value (through income) after the acquisition date. Contingent consideration classified as equity would not be remeasured. To determine whether contingent consideration represents a liability or equity, an entity should consult other applicable literature, such as Statement 133, Statement 150, and Issue 00-19.

Example

Assume that an acquirer agrees to pay an additional $6 million in cash to the previous owner if cumulative net income of the acquired business reaches $10 million within three years of the acquisition date. Further assume that the fair value of the contingent consideration as of the acquisition date is $4 million. At the end of each reporting period after the acquisition date, the contingent payment is remeasured to its fair value, with changes in fair value recorded through the income statement. For example, if the likelihood of meeting the target increases, the fair value of the contingent consideration increases. If the target is met and the $6 million contingent consideration is payable, cumulatively $2 million will have been recorded in the income statement (the difference between the $6 million payment and the $4 million originally recorded in the fair value allocation) by the time the $6 million is paid. Conversely, if the contingency is not met or its fair value declines, any accrued liability would be reversed into income.

If, however, the contingent consideration meets the conditions for classification as equity, then the fair value of the contingent consideration would not be remeasured after the acquisition date. In addition, if the target is not met, the amount originally recorded in equity for the contingent consideration would not be reversed.

10. What are replacement share-based payment awards?

Replacement share-based payment awards are issued by the acquirer to employees of the acquired entity only to replace their existing share-based payment awards that are tied to the acquired entity's stock (e.g., stock options). Replacement awards are subject to special business combination accounting, described in Question 11.

Awards granted by the acquirer that do not replace existing acquiree awards would be accounted for as share-based compensation in the postcombination financial statements.

Example

The CEO of an acquired company holds 1,000 previously granted stock options on the acquired company's stock. As of the acquisition date, the acquirer (1) replaces the 1,000 options currently held by the CEO with 1,000 options on the acquirer's stock (adjusted for the exchange ratio) and (2) grants an additional 500 options on the acquirer's stock. The 1,000 options granted by the acquirer to replace previously held options are considered "replacement options" subject to the provisions of Statement 141(R). The additional 500 options are not replacement options and, instead, would be accounted for as compensation under Statement 123(R).

11. How are replacement share-based payment awards accounted for under Statement 141(R)?

On this issue, Statement 141(R)'s guidance is consistent with current practice. First, if the fair-value-based measure of the acquirer's replacement awards is greater than the fair-value-based measure of the replaced awards as of the acquisition date, the difference is expensed in future earnings.

Second, the fair-value-based measure of the replaced awards is split into two portions: (1) a portion attributable to past services and (2) a portion attributable to future services. The portion attributable to past services is included in the consideration transferred for the acquired business. The portion attributable to future services is recognized as expense, since the services are provided after the acquisition date. This is true regardless of whether the acquired entity's employees had performed all services required to earn the original awards. In addition, if an acquirer replaces awards of an acquiree that expire as a result of a business combination even though there is no obligation to do so, the entire amount assigned to those awards would be recognized as compensation expense in the postcombination financial statements.

The fair value of all awards is calculated in accordance with Statement 123(R). Deferred tax assets can be recognized for the portion of share-based payment awards classified as equity and related to past service, if they ordinarily would result in future tax deductions for the acquirer.

Example

Target Company issues 100 stock options to an employee on January 1, 2008, that cliff vest after three years (i.e., on January 1, 2011).

On January 1, 2009, Parent Company acquires Target Company and replaces the 100 options on Target Company's stock with 100 options on its own stock. The fair-value-based measure of both the Parent Company options and the Target Company options on January 1, 2009, is $10 per option. In this example, the replacement options retain the original vesting conditions.

The total fair-value-based measure of the options as of the acquisition date is $1,000, of which $333 (one of three years) is attributable to past services and $667 (two of three years) is attributable to future services. The $333 is included in the consideration transferred, and $667 is recognized as compensation cost by Parent Company as the services are performed (i.e., from January 1, 2009, to January 1, 2011). Note that the original value assigned to the options by Target Company has no relevance as of the acquisition date.

12. How are business combinations that are achieved in stages (sometimes referred to as step acquisitions) accounted for under Statement 141(R)?

"Step acquisitions" occur when control of a business is obtained after the acquirer already owns a noncontrolling interest in the acquiree's equity. Under Statement 141(R), in a step acquisition, the acquirer's preexisting interest in the acquiree is remeasured to its fair value, with a resulting **gain or loss recorded in the income statement upon consummation of the business combination**. After the preexisting interest is remeasured to fair value, it is included in the fair value of the entire business acquired.

Furthermore, once control is obtained, acquisitions and dispositions of noncontrolling interests in the subsidiary are accounted for as equity transactions under Statement 160 (i.e., as long as control is retained, subsequent acquisitions and dispositions of equity interests will **not** result in a gain or loss).

Example

Acquirer purchases a 35 percent interest in Target Company for $2,000 on January 1, 2008. Acquirer uses the equity method to account for its 35 percent interest in Target Company. Assume that Acquirer's equity in the income of Target Company from January 1, 2008, to the end of December 31, 2009, is $500; as a result, the book value of Acquirer's interest in Target Company as of December 31, 2009, is $2,500.

On December 31, 2009, Acquirer purchases an additional 40 percent of Target Company for $4,000. Assume that on December 31, 2009, the total fair value of Target Company is $10,000 (this example assumes no control premium) and the fair value of 35 percent of Target Company is $3,500. On December 31, 2009, Acquirer's existing 35 percent interest in Target Company is remeasured to $3,500, resulting in a gain of $1,000 ($3,500 less the $2,500 book value) in the income statement. On December 31, 2009, Acquirer would then account for the acquisition of control of Target Company as a business combination in which the fair value of 100 percent of Target Company is $10,000 and the fair value of 75 percent of Target Company is $7,500.

If Acquirer purchases (or disposes of) additional interests in Target Company in the future (provided that control was retained), those interests would be accounted for as equity transactions — no assets or liabilities would be remeasured at fair value, and no gains or losses would be recognized.

Assets Acquired and Liabilities Assumed

13. Why did the FASB change the terminology of accounting for a business combination from the "purchase method" to the "acquisition method"?

Statement 141(R) indicates that a business combination can occur when a purchase does not occur (e.g., an entity's repurchase of a sufficient number of its own shares for an existing investor to obtain control or a lapse of minority veto rights that previously kept the acquirer from controlling an acquiree). The FASB changed the terminology because it believes that the term "acquisition method" is more representative of the types of transactions that result in a business combination.

14. Which assets acquired and liabilities assumed in a business combination are not recognized at fair value?

Generally, under Statement 141(R), more assets acquired and liabilities assumed in a business combination must be measured at fair value than under Statement 141. Like Statement 141, the new standard stipulates use of other applicable GAAP for measuring certain assets and liabilities. In addition, Statement 141(R) introduces new exceptions to the fair value measurement principle. The following assets and liabilities are not measured at fair value under Statement 141(R):

Carryforward From Statement 141:

- **Income Taxes** — Deferred tax assets and liabilities are measured in accordance with Statement 109; income tax uncertainties are measured in accordance with Interpretation 48.
- **Employee Benefits** — Assets and liabilities are measured in accordance with other applicable GAAP (e.g., Opinion 12, Statement 87, Statement 106).
- **Share-Based Payment Awards** — A liability or equity instrument related to the replacement of an acquiree's share-based payment awards with share-based payment awards of the acquirer is measured in accordance with Statement 123(R).
- **Assets Held for Sale** — Measured at fair value less cost to sell in accordance with Statement 144.

New Guidance in Statement 141(R):

- **Indemnification Assets** — The acquiree may indemnify the acquirer for the outcome of a contingency or uncertainty related to an asset or liability. Statement 141(R) requires that the indemnification asset be recorded at the same amount as the liability (less any contractual limitations or an allowance for collectibility), which may not be fair value (see Question 15).

- **Reacquired Rights (e.g., License or Franchise)** — The intangible asset recognized is measured on the basis of the remaining contractual term of the related contract, regardless of whether market participants would consider potential contractual renewals in determining the asset's fair value (see Question 19).

15. What is an acquired indemnification asset and how should it be accounted for in a business combination?

In a business combination, the seller may indemnify the acquirer for the resolution of a contingency or uncertainty that relates to a specific asset or liability. For example, the seller may indemnify the acquirer for specified losses over a certain dollar threshold that are associated with a lawsuit that predated the business combination. In this case, the acquirer has acquired an indemnification asset as part of the business combination. As discussed in Question 14, Statement 141(R) requires that the asset be recorded at the same amount as the liability (less any contractual limitations or an allowance for collectibility), even if this measure is not fair value.

Example

On June 15, 2009, Company A acquired 100 percent of Company B. Before the acquisition, B had a $100 liability related to an uncertain tax position that was recognized in accordance with Interpretation 48. In applying the acquisition method of accounting, A must follow Interpretation 48 and, therefore, recognize a $100 liability related to B's uncertain tax position (A agreed with B's analysis regarding the uncertain tax position). As part of the acquisition, the former owners of B agreed to indemnify A for any losses related to the tax position (including the $100 liability recognized by A). Statement 141(R) requires that A record an indemnification asset at the same amount as the liability, $100 (this assumes that collectibility is not in doubt), even though this amount most likely does not represent fair value (i.e., the measurement requirements of Interpretation 48 are not fair-value-based).

16. Can valuation allowances be reflected for assets that are recognized at fair value as of the acquisition date?

No. Separate valuation allowances will not be recognized on assets that are recorded at fair value as of the acquisition date. Statement 141(R) requires that receivables, including loans, be recorded at fair value. Fair value measurements incorporate assumptions regarding collections risk, obviating the need for a separate valuation allowance. Thus, the impact of an uncollectible receivable becoming collectible after the acquisition date is not recorded until receipt of payment. Under Statement 141, acquired loans and receivables are recorded at present amounts to be received, determined at appropriate current interest rates less allowances for uncollectibility and collection costs, if necessary.

17. Is an acquirer required to recognize assets that it does not intend to use or use in a way other than their highest and best use? If so, how should those assets be valued?

An acquirer may decide not to use an acquired asset for competitive or other reasons. For example, an acquirer may decide not to use an acquired brand name because it believes that its own brand is better positioned in the marketplace. If an acquirer decides not to use an acquired intangible asset, it is still required to recognize the asset and measure it at fair value in accordance with Statement 157. This valuation would need to reflect the asset's highest and best use, from a market participant's point of view, both as of the acquisition date and in subsequent impairment tests. Under current practice, these assets are typically assigned either no value or a value related only to the period of expected use.

18. Can an acquirer recognize a liability for restructuring costs related to the acquiree that it expects to incur as part of the business combination?

No. Costs that an acquirer expects to incur in the future that are related to its plans to exit an activity, involuntarily terminate employees, or relocate employees of an acquiree will not be assumed liabilities of the acquiree. In this regard, Statement 141(R) represents a significant change from current GAAP, under which acquirers may record liabilities for restructuring costs as long as the criteria in Issue 95-3 are met. Under Statement 141(R), if the acquiree has plans in place to exit an activity, involuntarily terminate employees, or relocate employees, such amounts will be considered liabilities assumed by the acquirer if the recognition criteria in Statement 146 are met.

19. Does Statement 141(R) provide any guidance on the recognition, measurement, and subsequent accounting for reacquired rights?

Yes. In a business combination, the acquirer may reacquire a right that had previously been granted to the acquiree (e.g., a license or franchise). Statement 141(R) stipulates that reacquired rights are identifiable intangible assets that must be recognized apart from goodwill. The asset would be measured on the basis of the remaining contractual term, regardless of whether market participants would take into account renewals in the fair value determination. Therefore, in these situations, reacquired rights will not be measured at fair value in accordance with Statement 157. In addition, if the terms of the contract give rise to a reacquired right that is favorable or unfavorable to market, then the acquirer will recognize a settlement gain or loss. Statement 141(R) requires that the asset, once acquired, be amortized over the remaining contractual period. Finally, if the intangible asset is sold to a third party, the carrying amount would be included in the gain or loss on sale.

20. What is acquired in-process research and development (IPR&D), and how is it accounted for under Statement 141(R)?

Entities acquired in a business combination often expend a significant amount of resources on product development before the acquisition date. These research and development expenditures may result in the development of certain intangible assets by the acquired entity, which would be expensed as incurred in accordance with Statement 2 (unless they had an alternative future use). In other words, an acquired entity would probably not record any assets on its books before the consummation of a business combination related to research and development. To the extent that the acquired entity was using, or was planning to use, these unrecognized assets for research and development activities, the assets would represent acquired IPR&D to the buyer.

Statement 141 requires that IPR&D assets be valued in the purchase price allocation and then immediately expensed. Under Statement 141(R), acquired IPR&D assets will not be immediately expensed. Rather, under Statement 142 (as amended by Statement 141(R)), acquired IPR&D will be accounted for as an indefinite-lived intangible asset until completion or abandonment of the associated research and development efforts. Therefore, these assets would not be amortized, but would be tested for impairment at least annually. Once the research and development activities are completed, the related assets would be amortized over the related product's useful life. If the project is abandoned, the assets would be written off if they have no alternative future use.

Statement 141(R) does not change the accounting for research and development expenditures incurred outside of a business combination. Therefore, any research and development expenditures incurred after the acquisition date that relate to an acquired IPR&D project would generally be expensed as incurred.

21. If control is obtained, but less than 100 percent of a business is acquired, how does Statement 141(R) change the determination of the amounts assigned to identifiable assets acquired and liabilities assumed?

Statement 141(R) explains that companies need to record 100 percent of the identifiable assets acquired and liabilities assumed when control is obtained, even if less than 100 percent of a business is acquired. This differs from current GAAP, which require that only the controlling interest's share of the assets acquired and liabilities assumed be recognized at fair value and the remainder at book value. The FASB reasoned that once an acquirer obtains control of an entity, it controls all of an asset, not a portion of it.

As a basic example, if the fair value of the acquired business's net assets was $100 and the acquirer purchased 80 percent of the business, Statement 141(R) would require the acquirer to consolidate $100 worth of net assets in its financial statements as of the acquisition date. However, under current GAAP, if we assume that the net assets acquired have a book value of $60 as of the acquisition date, the acquirer would consolidate only $92 of net assets (80 percent of $100 plus 20 percent of $60).

Under Statement 141(R), an acquisition of a controlling interest in another entity that is less than 100 percent will most likely result in a greater amount of depreciation and amortization expense in the postcombination income statement than would have been recognized under Statement 141.

22. How are noncontrolling interests in an acquired business measured in the fair value allocation?

Noncontrolling interests in the acquired business will be measured initially as its share in the fair value (instead of book value, as currently required) of the identifiable assets acquired and liabilities assumed, plus its share of goodwill. See the example in Question 27.

23. Does Statement 141(R) change how intangible assets are recognized apart from goodwill?

Generally, no. In a manner consistent with current GAAP, Statement 141(R) indicates that as long as the intangible asset acquired is *identifiable*, the intangible asset should be recognized separately from goodwill in the fair value allocation. An intangible asset is identifiable if it (a) arises from contractual or other legal rights or (b) is capable of being separated or divided from the acquired entity and sold, transferred, licensed, rented, or exchanged.

Note that Statement 141(R) provides guidance on the recognition of certain assets that may not have been recognized under Statement 141. For example, Statement 141(R) requires an entity to recognize an intangible asset for an acquired asset that an entity does not intend to use (see Question 17). In addition, Statement 141(R) changes the accounting for acquired IPR&D (see Question 20) in that an asset will be recognized in postacquisition periods. This treatment differs from that of Statement 141, which required immediate expensing of the IPR&D asset.

24. How are contingent assets acquired and contingent liabilities assumed accounted for under Statement 141(R)?

Under Statement 141(R), an acquirer must first determine whether contingent assets acquired and liabilities assumed are contractual or noncontractual. All contractual contingencies are recognized at fair value as of the acquisition date. Noncontractual contingencies are recognized at fair value only if it is more likely than not, as of the acquisition date, that the contingency gives rise to an asset or liability, as defined in Concepts Statement 6. In other words, an acquirer recognizes a noncontractual contingent liability at fair value as of the acquisition date if there is a greater than 50 percent chance that the acquirer has assumed a present obligation. An acquirer should account for a noncontractual contingency that does not meet this criterion in accordance with other GAAP. Currently, such preacquisition contingencies are generally accounted for under Statement 5, which often means that no amount is recorded as of the acquisition date.

A contingent liability recognized as of the acquisition date should subsequently be measured at the higher of the acquisition-date fair value or the amount that would be recognized under Statement 5. A contingent asset recognized as of the acquisition date should subsequently be measured at the lower of the acquisition-date fair value or the best estimate of its future settlement amount. An acquirer would not derecognize the contingent asset or liability if it subsequently falls below the more-likely-than-not threshold. Rather, a contingent asset would be derecognized when it is collected or sold or when its rights are lost, whereas a contingent liability would be derecognized when it is settled or the obligation to settle is canceled or expires.

Example 1

On June 30, 2009, Company A acquires Company B. Before the acquisition, B's consumers served B with a class action lawsuit regarding the safety of its products, seeking damages of $5 billion. As of the acquisition date, Company A believes, partly on the basis of the resolution of similar lawsuits with its competitors, that there is only a 30 percent chance that it will be found liable. Since this is a noncontractual contingency and it is not more likely than not that A has assumed a present obligation, no amount would be recorded for the contingent liability as of the acquisition date.

Example 2

Assume the same facts as in Example 1, except that as of the acquisition date A believes there is a 55 percent chance that it will be found liable. In this case, because it is more likely than not that the acquirer has assumed a present obligation, it must record the fair value of the contingent liability (assume $2 billion) as of the acquisition date.

Example 3

Assume the same facts as in Example 2, except that one year has passed since the acquisition date. As a result of an unfavorable court ruling against one of its competitors, A now believes there is a 95 percent chance that it will be found liable; its best estimate of the amount of exposure is $3 billion. In accordance with Statement 141(R), A must increase the contingent liability recorded by $1 billion to $3 billion (since this represents A's best estimate of the payment) because the amount required to be recorded under Statement 5 exceeds the acquisition-date fair value of the liability.

Assessing What Is Part of the Exchange for the Acquiree

25. Does Statement 141(R) clarify which parts of the transaction price (or other payments made by the acquirer) should be included in the business combination accounting and which should not?

Yes. The acquirer is required to assess whether any portion of the transaction price (or other payment) is not part of the exchange for the acquiree. Statement 141(R) indicates that if a portion of the transaction price (or other payment) was arranged for the economic benefit of the acquirer or the combined entity, the payment is not part of the exchange for the acquiree. If not part of the exchange, the payment or a portion of the payment would not be included in the acquisition method accounting and would be expensed rather than added to goodwill.

The following are examples of other payments made by the acquirer that would be excluded from the exchange:

- Payments made to the acquiree's employees or former owners for future services.
- Payments made to settle certain preexisting relationships (e.g., if the acquisition effectively settles a lawsuit or supply arrangement between the acquirer and acquiree). Issue 04-1 has been nullified, and its consensus has been incorporated into Statement 141(R).
- A transaction that reimburses the acquiree or its former owners for paying the acquirer's acquisition-related costs (see Question 7).

Goodwill

26. Does the definition of goodwill change under Statement 141(R)?

Yes. While goodwill under Statements 141 and 141(R) is defined and measured as a residual, it will now be the residual of the fair value of the acquiree over the fair value of assets acquired and liabilities assumed. It will no longer be the residual of cost over the fair value of assets acquired and liabilities assumed. The result? Goodwill would represent goodwill of the entire acquired entity instead of only the controlling interest's portion. Therefore, in the estimation of a business's fair value, that fair value includes an implied amount for goodwill. If less than 100 percent of a business is acquired, a portion of the goodwill would be attributable to the noncontrolling interest.

27. How is goodwill allocated to the controlling interest and noncontrolling interests?

Goodwill allocated to the **controlling interest** is measured as the excess of (1) the fair value of the controlling interest's portion of the business acquired over (2) the controlling interest's percentage share of the fair value of net assets acquired. Goodwill allocated to the **noncontrolling interests** is measured as the difference between all the goodwill of the acquired business and the goodwill allocated to the controlling interest. Therefore, goodwill allocated to the controlling and noncontrolling interests will not always be proportional to the percentages owned. For example, this situation could occur when the acquirer pays a premium to obtain control of the acquiree (see Question 5).

Example

Assume the following:

- Acquirer purchases 65 percent of Target Company for $750.
- The total fair value of Target Company is $1,100.
- Sixty-five percent of the fair value of Target Company is $750 (equal to the purchase price).
- The fair value of Target Company's identifiable assets acquired, net of liabilities assumed, is $800.

The calculation of goodwill is as follows:

Fair value of 100 percent of Target Company	$ 1,100
Fair value of 100 percent of net assets of Target Company	(800)
Goodwill of 100 percent of Target Company	**$ 300**
Fair value of 65 percent of Target Company	$ 750
Fair value of 65 percent of net assets of Target Company (65% × $800)	(520)
Goodwill — controlling interest	**$ 230**
Goodwill — noncontrolling interest ($300 – $230)	**$ 70**

Note that the controlling interest's share of goodwill is not 65 percent of the total amount of goodwill.

Also note that the noncontrolling interest included in the fair value allocation would be $350 [(35% × $800, the fair value of net assets) + $70 goodwill].

Bargain Purchases

28. What is a bargain purchase?

While not expected to be common, a bargain purchase occurs when the aggregate of the fair value of the (1) consideration transferred, (2) noncontrolling interests in the acquiree, and (3) acquirer's previously held equity interest in the acquiree is less than the fair value of the net assets acquired. A bargain purchase may occur if the acquired entity is purchased in a forced liquidation or distress sale, for example.

29. How is a bargain purchase accounted for?

First, Statement 141(R) requires the acquiring entity to double-check its calculations before concluding that a bargain purchase exists. If the same conclusion is reached, any further excess **is recognized as a gain in the income statement** as of the acquisition date.

This is a change to current GAAP, in which no gain is recorded until certain other noncurrent assets acquired (e.g., intangible, long-lived, and other noncurrent assets) are reduced to zero. Also, any gains from bargain purchases are classified as extraordinary under current GAAP, whereas under Statement 141(R) they will be recorded as a component of operating income.

Example

Company A acquires 100 percent of Company B for $50 million in cash. Company A calculates the fair value of the net assets acquired as follows:

Investments	$	90 million
Building		50 million
Trademark		50 million
Less: liabilities		(10 million)
Fair value of B's net assets	$	180 million

After examining the $180 million fair value estimate again, A concludes that its measurements appropriately reflect consideration of all available information as of the acquisition date. Therefore, under Statement 141(R), A would record a $130 million gain ($180 million – $50 million) in its income statement as of the acquisition date.

In comparison, Statement 141 requires A to reduce the value it assigned to the building and trademark down to $0 ($100 million total reduction). Then, A would recognize an extraordinary gain of $30 million ($180 million – $100 million – $50 million).

Note: This example is intended to illustrate the difference in accounting between Statements 141 and 141(R) regarding bargain purchases. It is not intended to illustrate the potential magnitude of a gain that could be recognized in a bargain purchase.

Measurement Period

30. What is a measurement period?

The measurement period is the period after the consummation of a business combination during which the acquirer gathers information necessary to complete the business combination accounting (e.g., fair value of assets acquired and liabilities assumed, fair value of consideration transferred, fair value of the acquiree). The measurement period is generally consistent with the *allocation period* of Statement 141.

The measurement period for a particular asset or liability ends as soon as the acquirer receives the necessary information about the facts and circumstances that existed as of the acquisition date. In addition, the measurement period is limited to a maximum of one year from the acquisition date.

31. If, during the measurement period, an adjustment is made to the provisional amounts assigned to identifiable assets acquired and liabilities assumed (as contemplated in the previous question), how is that adjustment reported?

Statement 141(R) requires an acquirer to revise comparative prior-period information for any adjustments to provisional amounts (recorded as of the acquisition date). In addition, the acquirer can adjust provisional amounts only if it receives new information about facts and circumstances that existed as of the acquisition date. Statement 141(R)'s requirement to revise comparative information for prior-period financial information represents a significant change from prevailing practice under current GAAP, in which adjustments to provisional amounts are generally accounted for prospectively when the new information is received.

Example

Company A acquires 100 percent of Company M on November 1, 2009. Company A has a fiscal year-end of December 31. As part of the acquisition of M, A hired an independent appraisal firm to value the assets acquired and liabilities assumed (the "net assets"). This appraisal is not complete before A issues its financial statements for the year ended December 31, 2009. Therefore, A makes a provisional allocation to the net assets when filing its December 31, 2009, financial statements. As part of this provisional allocation, the acquired property, plant, and equipment (PP&E) is assigned a value of $450,000. This PP&E has a remaining useful life of three years as of the acquisition date.

Company A receives the final appraisal of the net assets on April 1, 2010. In the appraisal, the fair value of the PP&E as of the acquisition date is determined to be $480,000. Therefore, A is required to retrospectively adjust its 2009 financial information as follows:

- PP&E is increased on December 31, 2009, by $28,333, calculated as the $30,000 increase in the fair value of the PP&E, less $1,667 of additional depreciation expense that would have been recorded had the revised fair value been used as of the acquisition date.

- Goodwill is decreased by $30,000 on December 31, 2009.
- Depreciation expense for the year ended December 31, 2009, is increased by $1,667, representing the additional depreciation expense for 2009 on the basis of the revised fair value of the PP&E.

In addition, A is required to make the following disclosures:

- In the financial statements for the year ended December 31, 2009, a statement that the allocation of fair value to the net assets is not yet complete, since the final valuation report has not yet been received.
- In the financial statements for periods after December 31, 2009, the amounts of, and explanations for, the adjustments to the provisional allocations to PP&E recognized in the current period.

Income Taxes

32. Does Statement 141(R) provide guidance on changes in the acquired entity's deferred tax assets and uncertain tax position balances subsequent to the business combination?

Yes. If an acquired entity's deferred tax assets or uncertain tax position balances are adjusted during the measurement period because of new information about facts and circumstances that existed as of the acquisition date, goodwill should be adjusted. If, as a result, goodwill is reduced to zero, any further amounts are recorded to income tax expense. However, even during the measurement period, if the adjustment to the acquired deferred tax assets or uncertain tax position balances directly results from an identifiable event that occurred after the business combination, then the entire adjustment is made to income tax expense rather than an initial adjustment being made to goodwill.

After the measurement period, any changes in acquired deferred tax assets and uncertain tax position balances are recorded to income tax expense in the income statement. Under current GAAP, such changes in the acquired entity's deferred tax assets and uncertain tax position balances (except for changes in valuation allowances for acquired deferred tax assets) are generally recorded through goodwill, regardless of whether such changes occur during the allocation period. The requirement to record such adjustments through income tax expense is not limited to transactions consummated after the effective date of Statement 141(R). Rather, under the transition provisions of Statement 141(R), the new requirement applies to all business combinations, regardless of the consummation date. In other words, this requirement is the one transition provision that could affect future accounting for transactions occurring before Statement 141(R)'s effective date (see Question 2, Example 2).

Other

33. How are reverse acquisitions accounted for?

Statement 141(R)'s guidance on accounting for reverse acquisitions is consistent with current practice. In a reverse acquisition, the legal *acquiree* is identified as the accounting *acquirer* and the legal *acquirer* is the accounting *acquiree*. A reverse acquisition may occur, for example, when the legal parent issues so many shares to the previous owners of the acquired entity that the acquired entity receives the larger portion of the voting rights in the combined entity.

In a reverse acquisition, the legal subsidiary's financial statements reflect the acquisition of the legal parent just like any other purchase. However, the equity section of the legal subsidiary's financials is adjusted to reflect the capital structure of the legal parent (the acquiree).

A unique feature of reverse acquisitions is that noncontrolling interests must be measured as the noncontrolling interest's share in the book value of the legal subsidiary's net assets (versus fair value in other acquisitions).

34. How does the parent company account for acquisitions of noncontrolling interests?

Under Statement 160, acquisitions of noncontrolling interests are accounted for as equity transactions instead of under the Statement 141 purchase method (see Appendix B, Question 7).

35. Does Statement 141(R) affect the accounting for leveraged buyouts (LBOs) and leveraged recapitalizations?

Yes and no. Statement 141(R) nullifies Issue 88-16, thereby eliminating the complex accounting model for LBOs. Statement 141(R) will not, however, affect leveraged recapitalizations.

Appendix B

Q&As Related to Statement 160 (Noncontrolling Interests in Consolidated Financial Statements)

Click a question below to jump to its related Q&A.

Scope

1. What is the scope of Statement 160?*
2. When should financial statements be consolidated?*
3. What is a noncontrolling interest?*

Effective Date and Transition

4. What are the effective date and transition provisions of Statement 160?

Consolidated Financial Statements and Noncontrolling Interests

5. Does Statement 160 change how consolidated financial statements are prepared?*
6. How are net income and other comprehensive income allocated between controlling and noncontrolling interests?*
7. What is the accounting for changes in the parent's ownership percentage when the parent already has (and will continue to have) control?*
8. When a parent company loses controlling ownership in a subsidiary, what is the accounting?*
9. Should a series of transactions in which a parent is selling its controlling interest in a subsidiary be accounted for as a single transaction?
10. Does Statement 160 provide guidance on when to deconsolidate a subsidiary?
11. Does consolidated earnings per share include net income attributable to noncontrolling interests?*

* The FASB's redeliberations of the Exposure Draft that preceded Statement 160 did not result in many changes to the provisions included in the final statement. Therefore, questions marked with an "*" have been carried forward generally unchanged from Deloitte & Touche LLP's June 30, 2005, *Heads Up*.

Scope

1. What is the scope of Statement 160?

Statement 160 applies to all entities, except for not-for-profit organizations (which will continue to apply the "pre-amended" version of ARB 51). While Statement 160 carries forward much of ARB 51's guidance on preparing consolidated financial statements, it does significantly change the accounting for noncontrolling interests and deconsolidation of a subsidiary (see Questions 5–10).

2. When should financial statements be consolidated?

In a manner consistent with current GAAP, Statement 160 requires that financial statements be consolidated when one entity controls another. Usually, control is demonstrated by ownership of greater than 50 percent of the voting common stock of an entity. However, under Interpretation 46(R), consolidation may be required when less than 50 percent of voting common stock is owned (i.e., by a primary beneficiary).

3. What is a noncontrolling interest?

Currently referred to as a "minority interest," a noncontrolling interest is the portion of a subsidiary's equity that is attributable to the owners of the subsidiary other than its parent or its parent's affiliates. That subsidiary is controlled by its parent and is included in its parent's consolidated financial statements. Typically, noncontrolling interests own less than 50 percent of an entity. However, in the case of a variable interest entity under Interpretation 46(R), a noncontrolling interest holder might own more than 50 percent of the voting stock of the entity (even up to 100 percent) because the controlling entity exercises control by other means.

Effective Date and Transition

4. What are the effective date and transition provisions of Statement 160?

Statement 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Early adoption is prohibited. However, application of Statement 160's disclosure and presentation requirements is retroactive, including:

- Reclassifying noncontrolling interest as a separate component of shareholders' equity.
- Adjusting consolidated net income and comprehensive income to include amounts attributable to both controlling and noncontrolling interests.
- Allocating consolidated net income and the components of other comprehensive income pursuant to Statement 160 (see Question 6).
- Allocating and disclosing income from continuing operations, discontinued operations, and extraordinary items related to the controlling interest.
- Reconciling the beginning and ending carrying amounts of total equity, equity attributable to the parent, and equity attributable to the noncontrolling interest (including separate disclosure of net income, transactions with owners, and each component of other comprehensive income).
- Disclosing the effects of any changes in a parent's ownership interest in a subsidiary on the equity attributable to the parent.
- Disclosing the amount of any gain or loss recognized for all periods presented if control of a subsidiary was lost before adoption of Statement 160, including the income statement caption in which it was presented and the portion that relates to the remeasurement of any retained investment in the former subsidiary at fair value.

Consolidated Financial Statements and Noncontrolling Interests

5. Does Statement 160 change how consolidated financial statements are prepared?

Yes and no. Statement 160 retains the general consolidation accounting procedures, including the following:

- Intercompany transactions are eliminated upon consolidation.
- Results of operations from the date control is obtained (usually the acquisition date) are included in consolidated retained earnings (deficit).
- Net income attributable to noncontrolling interests is deducted from consolidated net income.

However, there are two key changes. First, accumulated losses attributable to noncontrolling interests can exceed the original investment in the noncontrolling interest. That is, a noncontrolling interest can be in a debit position (i.e., negative noncontrolling interest). While this change is prospective, Statement 160 requires pro forma disclosures, in the year of adoption, to show any significant impact this change will have on the controlling interest's share of net income and earnings per share. Second, noncontrolling interests are now a component of shareholders' equity. Under current GAAP, companies generally record noncontrolling interests as either "mezzanine" (or temporary) equity or a liability.

6. How are net income and other comprehensive income allocated between controlling and noncontrolling interests?

Both consolidated net income (loss) and other comprehensive income (loss) would be allocated to the controlling interest and noncontrolling interests on the basis of their relative ownership percentages unless there is an agreement that indicates otherwise, in which case the allocation would be based on that agreement.

One exception to proportional allocation occurs when goodwill impairments are included in the income statement, because goodwill allocated to the controlling interest and noncontrolling interest(s) may not always be proportional to their ownership percentages in the subsidiary (see Appendix A, Question 27).

7. What is the accounting for changes in the parent's ownership percentage when the parent already has (and will continue to have) control?

After control is obtained, additional purchases and sales of a subsidiary's stock are equity transactions. This means that no gain or loss will be recognized in consolidated net income or comprehensive income on these transactions (i.e., no more SAB 51 gains or losses); any difference between the consideration paid to acquire the additional interest and the book value of those interests is recorded in the controlling interest's equity (additional paid-in capital). Under Statement 160, these changes must be applied prospectively and prior transactions cannot be changed.

As background, SAB 51 (Topic 5.H) explains that under certain circumstances, when a parent company's percentage ownership decreases as a result of the subsidiary issuing additional shares of its own stock, gains may be recognized through the income statement.

Example 1

Parent Company owns 80 percent of its subsidiary, which has a net book value of $100. Assume that the noncontrolling interest in the subsidiary is $20 and the controlling interest is $80. Let's say that Parent Company buys out the remaining 20 percent of the subsidiary for $30.

When this transaction occurs, the noncontrolling interest (a component of equity) is reduced by $20 to zero and the equity of the controlling interest is reduced by $10. There are no changes to consolidated assets or liabilities except for the $30 cash paid for the additional interest. One way to view this transaction is to consider it to be similar to a treasury stock transaction.

The journal entry is:

	Debit	Credit
Noncontrolling interest in subsidiary (a component of consolidated equity)	$ 20	
Controlling interest — additional paid-in capital (a component of parent company and consolidated equity)	10	
Cash		$ 30

Example 2

Assume the same starting point as in Example 1. However, the parent does not buy out the noncontrolling interest; instead, the subsidiary issues stock to unrelated parties for total proceeds of $20. This brings the subsidiary's total book value to $120 but dilutes Parent Company's interest to, let's say, 75 percent (i.e., $90 and $30 to the controlling and noncontrolling interests, respectively).

When this transaction occurs, the noncontrolling interest increases by $10 to $30 and the controlling interest increases by $10 to $90.

The journal entry would be:

	Debit	Credit
Cash held by the subsidiary	$ 20	
Noncontrolling interest in subsidiary		$ 10
Controlling interest — additional paid-in capital		10

8. When a parent company loses controlling ownership in a subsidiary, what is the accounting?

In this situation, a gain or loss is recognized in consolidated net income. The gain or loss is calculated as the difference between the following:

- The fair value of the consideration received, fair value of the former parent's retained noncontrolling interest as of the date control was lost, if any, and the carrying value of the noncontrolling interest as of the date control was lost, if any.
- The book value of the former subsidiary's net assets before control was lost.

Example

Parent Company owns 80 percent of its subsidiary, with a book value of $100. Assume that (1) the book values of the noncontrolling interest and controlling interest are $20 and $80, respectively; (2) Parent Company reduces its interest in the former subsidiary to 10 percent by selling stock for $105; (3) the fair value of 100 percent of the subsidiary is $150 and the fair value of 10 percent is $15.

The gain on the sale would be computed as follows:

Fair value of consideration received (cash proceeds)	$ 105
Fair value of retained noncontrolling interest in the subsidiary	15
Carrying value of noncontrolling interest	20
	140
Less: subsidiary's book value	100
Gain on sale	$ 40

The journal entry would be:

	Debit	Credit
Cash	$ 105	
Investment in former subsidiary	15	
Noncontrolling interest in former subsidiary	20	
Net assets of former subsidiary		$ 100
Gain on sale		40

9. Should a series of transactions in which a parent is selling its controlling interest in a subsidiary be accounted for as a single transaction?

It depends. Statement 160 provides that the parent may be required to account for multiple transactions as a single transaction if any of the following four indicators are present:

- The transactions are entered into at the same time or in contemplation of one another.
- The transactions are designed to achieve an overall business plan.
- One of the transactions depends on the success of one or more other transactions.
- Any single transaction is not economically justifiable; however, this same transaction is economically justifiable when considered alongside all other transactions.

Statement 160 includes the above indicators to prevent abuse by companies that may attempt to minimize earnings implications when disposing of a subsidiary (e.g., a parent company that intended to sell a 100-percent-owned subsidiary at a loss). Without these indicators, the parent company may attempt to structure the sale in two transactions in a way that minimizes the sale's negative effect on earnings. In the first transaction, for example, the parent company may sell 49 percent. Since the parent company retains control, the loss would be recorded in equity and there would be no effect on earnings. In the second transaction, the parent company may sell the remaining 51 percent. However, since the parent company now loses control, this portion of the loss is recorded in the income statement.

The FASB also reminds companies that paragraph 28(e) of Statement 142 requires a company to perform a goodwill impairment test if the company believes that it more likely than not will sell a reporting unit or a significant portion of a reporting unit.

10. Does Statement 160 provide guidance on when to deconsolidate a subsidiary?

Yes. Statement 160 requires a parent company to deconsolidate a subsidiary when it ceases to have a controlling financial interest in the subsidiary, such as when:

- A parent sells all or a part of its ownership interest.
- A contractual agreement that gave control of the subsidiary to the parent expires.
- The subsidiary issues shares, which reduces the parent's interest in the subsidiary below a controlling amount.
- The subsidiary becomes subject to the control of a government, court, administrator, or regulator.

11. Does consolidated earnings per share include net income attributable to noncontrolling interests?

No. Statement 160 amends Statement 128 to explain that earnings per share is computed solely on the basis of net income attributed to the controlling interest's share of its subsidiaries' income. That is, income attributable to noncontrolling interests is excluded from the computation. This is no different from how earnings per share is currently calculated.

Appendix C

Comparison With Current U.S. GAAP

The following table lists key accounting differences between Statements 141(R) and 160 and current U.S. GAAP. Included are references to relevant questions and answers from Appendixes A and B.

Item	New Accounting	Current Accounting
Statement 141(R)		
Measurement date of equity securities issued (see Appendix A, Question 6)	Measure the fair value of the acquirer's equity securities issued as of the acquisition date.	Follow the guidance in Issue 99-12. Measure the fair value of equity securities issued a few days before and after the terms of the combination are agreed upon and announced.
Transaction costs of the acquirer (see Appendix A, Question 7)	Expense as incurred and exclude from the fair value of the business acquired (because they are not part of the fair value of the entity acquired).	Include in the cost of the acquired business; generally add to goodwill.
Contingent consideration (see Appendix A, Questions 8 and 9)	Include, in the acquisition accounting, at fair value (either as a liability or in equity, depending on its nature). For contingent consideration recorded as a liability, subsequent changes in fair value are recognized in the income statement (until settled). Contingent consideration recorded as equity is not subsequently remeasured.	Generally, record as an adjustment in the postcombination period when the contingency is resolved and the consideration is issuable. An amount is often not recognized as of the acquisition date, nor does resolution of the contingency result in an income statement impact.
Step acquisitions (see Appendix A, Question 12)	Record 100 percent of the fair value of the acquiree once control is obtained. A gain or loss is recognized on preexisting equity interest held by the acquirer.	When an acquirer has a preexisting equity interest in the acquiree, only record the fair value of the incremental interest that is acquired.
Indemnification assets (see Appendix A, Question 15)	Record at the same amount as the related contingent liability (less any contractual limitations or an allowance for collectibility), even if this measurement is not fair value.	Diversity in practice.
Valuation allowances for assets recorded at fair value (see Appendix A, Question 16)	Assets are recognized at fair value in accordance with Statement 157, with no separate valuation allowance.	Typically, assets are recognized at present value less a credit allowance.
Assets that an acquirer does not intend to use (see Appendix A, Question 17)	Record at fair value in accordance with Statement 157, reflecting the asset's highest and best use.	Typically, assets are either assigned no value or the value is related only to the period of expected use.
Restructuring costs (see Appendix A, Question 18)	Only restructuring costs of the acquiree that meet the recognition criteria in Statement 146 as of the acquisition date are included in the fair value allocation. All others are postcombination costs that are recognized in the income statement when incurred. Most restructuring reserves recognized under Statement 141 will not be recognized under Statement 141(R).	Restructuring costs are recognized as a liability in the purchase price allocation provided that certain conditions in Issue 95-3 are met.

Item	New Accounting	Current Accounting
In-process research and development (IPR&D) (see Appendix A, Question 20)	Under Statement 142, as amended by Statement 141(R), acquired IPR&D is capitalized as an indefinite-lived intangible asset until completion or abandonment of the project. Upon completion, the research and development asset is accounted for as a finite-lived intangible asset and amortized over the related product's estimated useful life. If the project is abandoned, the asset is expensed immediately if no alternative future use exists.	The fair value of IPR&D with no alternative future use is charged to expense as of the acquisition date.
Assets acquired and liabilities assumed (see Appendix A, Question 21)	When control is obtained, record at 100 percent of fair value (even if less than 100 percent is acquired).	Only the controlling interest's portion is recorded at fair value.
Preacquisition contingencies (see Appendix A, Question 24)	Contractual contingencies, and those noncontractual contingencies that more likely than not meet the definition of an asset or liability, are recognized at fair value as of the acquisition date. In subsequent periods, (1) a contingent asset is remeasured to the lower of its acquisition-date fair value or the best estimate of its future settlement amount and (2) a contingent liability is remeasured to the higher of its acquisition-date fair value or the amount that would be recognized under Statement 5. Subsequent changes in measurement are included in income.	Recognize at fair value, if determinable, during the allocation period. Otherwise, follow Statement 5 and recognize, if probable and the amount is reasonably estimable, during the allocation period. Often, no amount is recorded as of the acquisition date. Therefore, the impact of the settlement of a contingency is typically recorded in the postcombination income statement.
Goodwill (see Appendix A, Question 27)	Allocate to the controlling and noncontrolling interests.	Allocate only to the controlling interest.
Bargain purchase (see Appendix A, Questions 28 and 29)	Recognize a gain in the period the acquisition occurs. The gain is calculated as the excess of the fair value of the net assets acquired over the sum of (1) the fair value of the consideration transferred, (2) the fair value of any previously held equity interests, and (3) the fair value of any noncontrolling interests. There is no pro rata reduction of certain noncurrent assets.	The excess of the fair value of the net assets acquired over the fair value of the consideration transferred reduces certain noncurrent assets on a pro rata basis. Any amount of the excess that remains after these assets are reduced to zero is recognized as an **extraordinary** gain.
Adjustments made to the fair value allocation within the measurement period (see Appendix A, Question 31)	Comparative financial statements are revised as if the adjustments were made as of the acquisition date.	Generally, such adjustments are made prospectively.
Adjustments to acquired deferred tax assets and uncertain tax positions (see Appendix A, Question 32)	Adjustments that occur after the measurement period are recorded as a component of income tax expense. Adjustments during the allocation period would generally be recorded as a component of goodwill.	In accordance with Issue 93-7, generally recorded through goodwill (regardless of whether such adjustments occur during the allocation period).
Leveraged buyouts (see Appendix A, Question 35)	Issue 88-16 is nullified; account for transaction in accordance with Statement 141(R).	Follow the guidance in Issue 88-16.
Statement 160		
Noncontrolling interests (see Appendix A, Question 22)	Recognize the noncontrolling interest's share of **fair value** of net assets acquired, including its share of goodwill, as of the acquisition date.	Recognize the noncontrolling interest's share of book value of net assets acquired as of the acquisition date.

Item	New Accounting	Current Accounting
Accumulated net losses attributable to noncontrolling interests (see Appendix B, Question 5)	No longer limited to the original carrying amount of the noncontrolling interest (i.e., there can be a negative balance in noncontrolling interest as losses accumulate).	Cannot create a negative balance in noncontrolling interest.
Classification of noncontrolling interests (see Appendix B, Question 5)	Include as a separate component of shareholders' equity.	Classified as liability or mezzanine (or temporary) equity.
Increases and decreases in the ownership percentage of the subsidiary, as long as the parent retains control (see Appendix B, Question 7)	No gain or loss is recorded (i.e., no more SAB 51 gains or losses); changes in ownership are recorded as equity transactions.	Increases in ownership are accounted for under the purchase method. Decreases are recognized as sales of a portion of the subsidiary that generally result in gains or losses.

Appendix D

Key Changes Since the 2005 Exposure Drafts

In June 2005, the FASB issued two Exposure Drafts for comment. While the FASB reaffirmed many of its decisions from the Exposure Drafts, there were some significant changes, summarized below.

Item	Final Standards	Exposure Drafts
Statement 141(R)		
Effective date (Appendix A, Question 2)	Prospective application for years beginning on or after December 15, 2008. Earlier application is prohibited.	Prospective application for years beginning on or after December 15, 2006. Earlier application is permitted.
Allocating value of replacement share-based payment awards: consideration transferred versus postcombination earnings (Appendix A, Questions 10 and 11)	Fair value of acquirer's replacement award over acquiree's award is recognized in postcombination earnings. Fair value of both awards is calculated in accordance with Statement 123(R) and includes estimated forfeitures. Remainder of replacement award is allocated to consideration transferred on the basis of the ratio of the past service period to the greater of the total service period or original service period.	Fair value of acquirer's replacement award over acquiree's award is recognized in postcombination earnings. Fair value of both awards is calculated in accordance with Statement 123(R). Remainder of replacement award is allocated to consideration transferred on the basis of the ratio of the past service period to the total service period.
Recognition of deferred tax assets for replacement share-based payment awards classified as equity (Appendix A, Question 11)	If award would ordinarily result in a future tax deduction, recognize deferred tax asset for the portion of the replacement award related to past service and include in consideration transferred. Subsequent adjustments are generally recorded in equity.	Not specifically addressed.
Indemnification assets (Appendix A, Question 15)	Record at the same amount as the related contingent liability (less any contractual limitations or an allowance for collectibility), even if this measurement is not fair value.	Not specifically addressed.
Preacquisition contingencies (Appendix A, Question 24)	Recognize contractual contingencies, and those noncontractual contingencies that more likely than not meet the definition of an asset or liability, at fair value as of the acquisition date. In subsequent periods, (1) for a contingent asset, remeasure to the lower of its acquisition-date fair value or the best estimate of its future settlement amount and (2) for a contingent liability, remeasure to the higher of its acquisition-date fair value or the amount that would be recognized under Statement 5. Subsequent changes in measurement are included in income.	Recognize at fair value as of the acquisition date. Remeasure at fair value after the acquisition date until paid or otherwise settled.
Adjustments to acquired deferred tax assets and uncertain tax positions (Appendix A, Question 32)	If subsequent information received during measurement period relates to facts and circumstances that existed as of the acquisition date, adjust goodwill (until reduced to zero) and then income tax expense. Otherwise, adjust income tax expense.	Rebuttable presumption that postacquisition adjustments will first be to goodwill and any remaining amounts to income tax expense.
Leveraged buyouts (LBOs) (Appendix A, Question 35)	Issue 88-16 is nullified; account for transaction in accordance with Statement 141(R).	LBOs are not within the scope of Statement 141(R).

Item	Final Standards	Exposure Drafts
Disclosures — pro forma financial information	An acquirer that is a public company must disclose revenue, net income, and earnings per share for all periods presented.	An acquirer that is a public company must disclose revenue, results of operations, and earnings per share for all periods presented.
Disclosures — acquired contingencies	For contingent assets and liabilities, disclose nature of each acquired contingency (recorded or unrecorded), amount recognized, and estimated range of outcomes. Disclose subsequent changes in recognized amounts and estimated range of outcomes, including reasons for any changes.	For contingent liabilities assumed, disclose tabular reconciliation of beginning and ending balances, including changes in fair value and amounts paid or otherwise settled.
Disclosures — contingent consideration	Disclose amount recognized as of the acquisition date, along with description of the arrangement, the basis for determining outcomes, and the range of outcomes. After the acquisition date, disclose any changes in recorded amounts or ranges of outcomes.	Disclose tabular reconciliation of beginning and ending recorded balances until settled or paid.
Statement 160		
Effective date (Appendix B, Question 4)	Prospective application for years beginning on or after December 15, 2008. Early adoption is prohibited.	Prospective application for years beginning on or after December 15, 2006. Early adoption is permitted.
Increases or decreases in the ownership percentage of the subsidiary, as long as the parent retains control (Appendix B, Question 7)	Record prospectively after adoption of Statement 160. Amounts recognized for acquisitions or disposals of noncontrolling interests, including loss of control, before the adoption of Statement 160 cannot be changed.	Record retroactively after adoption of Statement 160.
Nonreciprocal transfers to owners (e.g., spin-offs)	Statement 160 clarifies that these transactions are not within its scope and that entities should continue to apply Opinion 29.	Not addressed.

Appendix E

Comparison With IFRSs

The table below highlights differences between the new FASB and the soon-to-be-issued IASB standards. Many of these differences arise from existing differences between U.S. GAAP and IFRSs, which the boards intend to address in future convergence projects (e.g., share-based payments and employee benefits), and did not directly arise as a result of the joint business combinations project.

Item	FASB Standards	IASB Standards
Effective date	Fiscal years beginning on or after December 15, 2008.	Annual periods beginning on or after July 1, 2009.
Early adoption	Prohibited.	Permitted.
Scope	Scope exception for not-for-profit organizations.	No scope exception for not-for-profit organizations.
Definition of control	A controlling financial interest, generally through ownership of a majority voting interest.	The power to govern the financial and operating policies of an entity to obtain benefits from its activities.
Definition of fair value	The price that would be received to sell an asset or that would be paid to transfer a liability in an orderly transaction between market participants as of the measurement date (paragraph 5 of Statement 157).	The amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's-length transaction.
Variable interest entities	The primary beneficiary must apply acquisition method accounting under Statement 141(R).	The IASB does not have an equivalent standard to the FASB's Interpretation 46(R).
Acquired leases in which the acquiree is the lessor	Recognize an intangible asset or liability separately from the leased asset if the terms of the lease are favorable or unfavorable, respectively, relative to current market terms or prices.	Favorable or unfavorable terms of the operating lease, relative to current market terms or prices, are embedded in the fair value measurement of the leased asset; no separate asset or liability is presented.
Acquired noncontractual contingencies — initial measurement	Recognize at fair value if the probability exceeds the more-likely-than-not threshold.	Recognize at fair value if it arises from a past event and can be measured reliably.
Acquired contingencies — subsequent measurement	For a contingent asset, record the lower of its acquisition-date fair value or the best estimate of its future settlement amount. For a contingent liability, record the higher of its acquisition-date fair value or the amount that would be recognized under Statement 5.	For a contingent liability, record the higher of the amount calculated under the best-estimate approach of IAS 37 or the acquisition-date fair value less cumulative amortization recognized under IAS 18 (if appropriate).
Noncontrolling interests — initial measurement	Measure at fair value. Disclose valuation techniques and significant inputs used.	Measure at fair value or proportionate share of acquiree's identifiable net assets (i.e., no goodwill allocated). Disclose measurement basis used.
Contingent consideration — initial recording	Classified as a liability or equity in accordance with existing standards (e.g., Statement 150), which are not converged with IFRSs.	Classified as a liability or equity in accordance with existing standards (e.g., IAS 39), which are not converged with U.S. GAAP.
Contingent consideration classified as liabilities — subsequent measurement	Remeasure at fair value.	Remeasure financial instruments at fair value. All other liabilities remeasured under IAS 37 using the best-estimate approach.

Item	FASB Standards	IASB Standards
Acquired deferred tax assets and uncertain tax positions	Recognize and measure in accordance with Statement 109 and Interpretation 48, which are not converged with IFRSs.	Recognize and measure in accordance with IAS 12, which is not converged with U.S. GAAP.
Employee benefits	Recognize and measure in accordance with existing standards (e.g., Statements 87 and 106), which are not converged with IFRSs.	Recognize and measure in accordance with IAS 19, which is not converged with U.S. GAAP.
Replacement share-based payment awards — initial measurement	Recognize and measure in accordance with Statement 123(R), which is not converged with IFRSs.	Recognize and measure in accordance with IFRS 2, which is not converged with U.S. GAAP.
Replacement share-based awards — allocating value to consideration transferred	Fair value of acquirer's replacement award over acquiree's award is recognized in postcombination earnings. Fair value of both awards is calculated in accordance with Statement 123(R) and includes estimated forfeitures. Remainder of replacement award is allocated to consideration transferred on the basis of the ratio of the past service period to the greater of the total service period or original service period.	Recognize fair value of acquirer's replacement award over acquiree's award in postcombination earnings. Allocate remainder of replacement award to consideration transferred on the basis of the ratio of the vesting period completed to the greater of the total service period or original vesting period.
Disclosures — pro forma financial information	Required only for public business enterprises; comparable prior-period disclosures must be presented.	Required for all acquirers for the current period only.
Disclosures — acquired contingencies	No explicit requirement to disclose major assumptions made concerning future events or the amount of expected reimbursements, if any.	Requirement to disclose major assumptions made concerning future events and the amount of expected reimbursements, if any.
Disclosures — gain or loss recognized on net assets acquired	No disclosure requirement.	Requirement to disclose amount and explanation of any gain or loss recognized in the current or prior period that relates to identifiable assets acquired and liabilities assumed in a business combination.
Disclosures — goodwill	For entities that apply segment reporting under Statement 131, requirement to disclose amount of goodwill allocated to each segment.	No requirement to disclose goodwill allocated to each cash-generating unit as of the acquisition date. However, requirement to disclose goodwill for each cash-generating unit as of the balance sheet date if significant compared with the entity's total goodwill under IAS 36 (revised).

Appendix F

Glossary of Standards

FASB Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements* — an amendment of ARB No. 51

FASB Statement No. 157, *Fair Value Measurements*

FASB Statement No. 150, *Accounting for Certain Financial Instruments With Characteristics of Both Liabilities and Equity*

FASB Statement No. 146, *Accounting for Costs Associated With Exit or Disposal Activities*

FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*

FASB Statement No. 142, *Goodwill and Other Intangible Assets*

FASB Statement No. 141(R), *Business Combinations*

FASB Statement No. 141, *Business Combinations*

FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*

FASB Statement No. 131, *Disclosures About Segments of an Enterprise and Related Information*

FASB Statement No. 128, *Earnings per Share*

FASB Statement No. 123(R), *Share-Based Payment*

FASB Statement No. 109, *Accounting for Income Taxes*

FASB Statement No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions*

FASB Statement No. 87, *Employers' Accounting for Pensions*

FASB Statement No. 5, *Accounting for Contingencies*

FASB Statement No. 2, *Accounting for Research and Development Costs*

FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* — an interpretation of FASB Statement No. 109

FASB Interpretation No. 46(R), *Consolidation of Variable Interest Entities* — an interpretation of ARB No. 51

Accounting Research Bulletin No. 51, *Consolidated Financial Statements*

APB Opinion No. 29, *Accounting for Nonmonetary Transactions*

APB Opinion No. 12, *Omnibus Opinion — 1967*, "Deferred Compensation Contracts"

EITF Issue No. 04-1, "Accounting for Preexisting Relationships Between the Parties to a Business Combination"

EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock"

EITF Issue No. 99-12, "Determination of the Measurement Date for the Market Price of Acquirer Securities Issued in a Purchase Business Combination"

EITF Issue No. 98-3, "Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business"

EITF Issue No. 95-3, "Recognition of Liabilities in Connection With a Purchase Business Combination"

EITF Issue No. 93-7, "Uncertainties Related to Income Taxes in a Purchase Business Combination"

EITF Issue No. 88-16, "Basis in Leveraged Buyout Transactions"

FASB Concepts Statement No. 6, *Elements of Financial Statements* — a replacement of FASB Concepts Statement No. 3 (incorporating an amendment of FASB Concepts Statement No. 2)

SEC Staff Accounting Bulletin No. 51, *Accounting for Sales of Stock by a Subsidiary*

IFRS 3 (revised), *Business Combinations*

IFRS 3, *Business Combinations*

IFRS 2, *Share-based Payment*

IAS 39, *Financial Instruments: Recognition and Measurement*

IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*

IAS 36, *Impairment of Assets*

IAS 27 (revised), *Consolidated and Separate Financial Statements*

IAS 19, *Employee Benefits*

IAS 18, *Revenue*

IAS 12, *Income Taxes*

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