

October 27, 2005

Technical Director  
Financial Accounting Standards Board  
401 Merritt 7  
P.O. Box 5116  
Norwalk, Connecticut 06856-5116

File Reference No. 1204-001

Re: Proposed Statement of Financial Accounting Standards  
*Business Combinations, a replacement of FASB Statement No. 141*

The Accounting Principles & Auditing Standards Committee of the California Society of Certified Public Accountants (the "Committee") submits the following comments on the proposed statement.

The AP&AS Committee is the senior technical committee of our state society. It has 43 members; 67 percent from local or regional firms, 23 percent sole practitioners in public practice, 5 percent from industry and 5 percent from academia.

The Committee discussed each of the questions posed to potential commenters. The outcomes of the Committee's discussions are noted as follows.

**Question 1** *Are the objective and the definition of a business combination appropriate for accounting for all business combinations? If not, for which business combinations are they not appropriate, why would you make an exception, and what alternative do you suggest?*

The Committee agrees with the objective and definition, including the exclusion of combinations involving entities under common control and the formation of joint ventures.

**Question 2** *Are the definition of a business and the additional guidance appropriate and sufficient for determining whether the assets acquired and the liabilities assumed constitute a business? If not, how would you propose to modify or clarify the definition or additional guidance?*

The Committee generally believes that the guidance on whether assets acquired and liabilities assumed constitute a business as presented in EITF Issue 98-3 has worked well in practice and disagrees that such guidance contains all of the shortcomings discussed in the Basis for Conclusions. The Committee also believes that an integrated set of

activities and assets managed to lower costs may not constitute a separate business for which acquisition accounting should be applied. For example, the Committee notes that certain plant acquisitions may qualify as a business following the proposed guidance and would, therefore, require the expensing of certain costs such as brokerage fees that, in the Committee's view, should be considered in the carrying amount of the acquired plant.

**Question 3** *In a business combination in which the acquirer holds less than 100 percent of the equity interests of the acquiree at the acquisition date, is it appropriate to recognize 100 percent of the acquisition-date fair value of the acquiree, including 100 percent of the values of identifiable assets acquired, liabilities assumed, and goodwill, which would include the goodwill attributable to the noncontrolling interest? If not, what alternative do you propose and why?*

The Committee agrees with the Board's conclusions.

**Question 4** *Do paragraphs A8-A26 provide sufficient guidance for measuring the fair value of an acquiree? If not, what additional guidance is needed?*

The Committee believes that the guidance is sufficient.

**Question 5** *Is the acquisition-date fair value of the consideration transferred in exchange for the acquirer's interest in the acquiree the best evidence of the fair value of that interest? If not, which forms of consideration should be measured on a date other than the acquisition date, when should they be measured, and why?*

The Committee agrees that the fair value of consideration transferred is the best evidence of the fair value of the interest acquired.

**Question 6** *Is the accounting for contingent consideration after the acquisition date appropriate? If not, what alternative do you propose and why?*

The Committee generally agrees with the accounting for contingent consideration after the acquisition date except for the contingent issuance of equity. The Committee notes that in many business combinations additional equity interests are issued based upon subsequent changes in the stock price. In those situations, the Committee agrees that equity consideration should not be remeasured since the additional issuance is based on events occurring subsequent to the acquisition date. However, in business combinations in which additional equity interests are issued in the resolution of a contingency such as the resolution of a lawsuit, additional equity consideration issued should be remeasured similar to liabilities.

**Question 7** *Do you agree that the costs that the acquirer incurs in connection with a business combination are not assets and should be excluded from the measurement of the consideration transferred for the acquiree? If not, why?*

A significant minority of the Committee believes that costs incurred in connection with a business combination are unavoidable and are a part of the fair value of the consideration transferred for the interests acquired. Those Committee members believe that the acquirer considers the costs of an acquisition in negotiating the terms of an acquisition and to exclude such costs would understate the fair value of the consideration. The majority of the Committee, however, believes that such costs do not meet the definition of an asset and should be expensed as incurred.

**Question 8** *Do you believe that these proposed changes to the accounting for business combinations are appropriate? If not, which changes do you believe are inappropriate, why, and what alternatives do you propose?*

The Committee generally agrees with the Board's conclusions regarding changes to Statement 141. However, some Committee members believe that the provisions of Statement 5 should continue to be used in recognition and measurement of contingencies since the proposed accounting will result in similar contingencies being recognized and measured differently in the consolidated financial statements of the combined entity, which will confuse financial statement users.

**Question 9** *Do you believe that these exceptions to the fair value measurement principle are appropriate? Are there any exceptions you would eliminate or add? If so, which ones and why?*

A minority of the Committee believes that the obligations for pensions and other post-employment benefits should be measured at fair value. However, a majority of the Committee believes that this exception should be given for the reasons discussed in the Basis for Conclusions.

**Question 10** *Is it appropriate for the acquirer to recognize in income any gain or loss on previously acquired noncontrolling equity investments on the date it obtains control of the acquiree? If not, what alternative do you propose and why?*

The Committee generally believes that it is inappropriate for the acquirer to recognize a gain or loss on previously acquired noncontrolling equity investments. The Committee believes that a more appropriate accounting would reflect the adjustment to fair value as an adjustment to equity, either directly as paid-in-capital or as other comprehensive

income. The Committee notes that the economic gains to the acquirer resulting from the business combination generally result from activities occurring after the acquisition date.

**Question 11** *Do you agree with the proposed accounting for business combinations in which the consideration transferred for the acquirer's interest in the acquiree is less than the fair value of that interest? If not, what alternative do you propose and why?*

The Committee agrees with the Board's conclusions.

**Question 12** *Do you believe that there are circumstances in which the amount of an overpayment could be measured reliably at the acquisition date? If so, in what circumstances?*

The Committee agrees that an overpayment cannot be reliably measured at the acquisition date.

**Question 13** *Do you agree that comparative information for prior periods presented in financial statements should be adjusted for the effects of measurement period adjustments? If not, what alternative do you propose and why?*

The Committee agrees with the Board's conclusions.

**Question 14** *Do you believe that the guidance provided is sufficient for making the assessment of whether any portion of the transaction price or any assets acquired and liabilities assumed or incurred are not part of the exchange for the acquiree? If not, what other guidance is needed?*

The Committee believes that the guidance is adequate.

**Question 15** *Do you agree with the disclosure objectives and the minimum disclosure requirements? If not, how would you propose amending the objectives or what disclosure requirements would you propose adding or deleting, and why?*

The Committee generally agrees with the objectives of disclosure and minimum disclosure requirements. However, with respect to paragraph 73(b), the Committee notes that the occurrence of certain events at or near issuance of the financial statements may make an impractical exception more reasonable than an impracticable one.

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**Questions 16-18** The Committee did not have sufficient time to discuss these issues.

**Question 19** *Do you find stating the principles in bold type helpful? If not, why? Are there any paragraphs you believe should be in bold type, but are in plain type, or vice versa?*

The Committee found the style of the exposure draft helpful and would be pleased to discuss its comments further with the Board or its staff.

Very truly yours,

Robert R. Coté, Chair  
Accounting Principles and Auditing Standards Committee  
California Society of Certified Public Accountants