



PUBLIC COMPANY FINANCIAL EXECUTIVE BRIEFING

New Accounting Rules for Mergers & Acquisitions

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Executive Summary

Effective for years beginning after December 15, 2008, new rules on accounting for all acquisitions of businesses become effective. The rules promulgated under Statements of Financial Accounting Standards Nos. 141 (R) and 160 (SFAS 141 (R) and 160) represent comprehensive changes in how business acquisitions and the activities related to them are accounted for, and have significant implications for the financial reporting teams in all companies. The rules move the accounting rules further along the road to fair value accounting and convergence with International Financial Reporting Standards (IFRS).

Major Changes and Practical Implications

The primary provisions in the new accounting standards and a very brief summary of the practical implications are as follows:

	Significant Provisions	Practical Implications
1	Expands the definition of what constitutes a Business	The expansion could increase significantly the number of acquisitions that fall under business combination rules and fewer that qualify as simple asset purchases.
2	Requires Companies to expense deal costs as incurred	Companies will now be required to write off most expenses as they occur. This includes Legal, Investment banking, Accounting, Printing and other transaction related costs.
3	Change the valuation date of the consideration to the date on which the acquirer obtains control of the target company	Transactions will no longer be valued at the date that the deal is struck, instead at the date that control transfers. This will most often be the closing date. This could cause significant fluctuations in values between when a deal is struck and when is recorded.

4	Companies may be required to value earn outs and acquisition date contractual contingencies at Fair Value	The value of earn outs and other contractual commitments will have to be valued at the date of the transaction. Additional subsequent costs or adjustments to those accruals will result in a charge to expense.
5	Restructuring costs the acquirer expects (but is not obligated) to incur are recognized separately from the acquisition	Under previous rules, certain restructuring costs expected to be incurred could be accrued as part of the acquisition accounting. Under the new rules, those costs would be accounted for under other guidance. Practical impact can be expected to be the recognition of restructuring costs as an expense in the financial statements when those costs are recognizable under the other appropriate guidance. No purchase price allocation value would be attributable to these costs.
6	Requires the non-controlling interest to be measured at fair value.	Because the non-controlling interest is measured at fair value, the amount of goodwill recognized is attributable to both the acquirer and the non-controlling interest. This accounting will likely result in higher goodwill values, which may have an impact on later impairment tests.
7	Requires that the entire excess of the acquisition-date fair value of identifiable net assets acquired over the fair value of consideration transferred plus, if applicable, the acquisition-date fair value of the non-controlling interest be recognized as a gain.	<p>Previous rules required so-called bargain purchase gains to be first allocated on a pro-rata basis to certain intangible and long term assets before recognizing the gain. The new rules require the assets to remain at their acquisition date fair values and then entire gain recognized immediately. The result is:</p> <ul style="list-style-type: none"> • A post-acquisition balance sheet that more truly represents the value of the acquired company, • Immediate gain recognition for the bargain, • Potential additional valuation models for assets and goodwill that previously may not have been recognized, and • On-going impairment reviews for those assets as well.
8	Requires In Process Research and Development (“IPRD”) be accounted for as a separately identified intangible asset and recorded as an asset of the acquisition	The new rules specify that IPRD be neither immediately written off nor amortized, but instead be subject to annual impairment testing, similar to the treatment of goodwill. When abandoned or impaired, the company would be required to take a loss for the write-down immediately.

9	Requires the acquirer to recognize assets or liabilities arising from non-contractual contingencies as of the acquisition date, measured at their acquisition-date fair values, if it is more likely than not that they meet the definition of an asset or a liability	Contingent liabilities assumed in an acquisition that previously were not recorded until the “Probable” criteria that was in place under existing accounting literature, may be required to be accrued on the date of the transaction. Also, under previous criteria, amounts were recognized only if estimable and then at the lower end of the range of possible outcomes. New guidance requires the amounts to be recorded at fair value which may require significant assumptions on the part of management.
10	Requires companies to record all of the profits or losses in the operations of subsidiaries where there is a non-controlling interest	Generally, previous rules stipulated that the income or loss attributable to the non-controlling interests in a subsidiary was backed out of the company’s income statements for purposes of computing net income or net loss. The new rules require those results to be incorporated with their own.

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