

January 27, 2016

Susan M. Cospers, CPA  
Technical Director  
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401 Merritt 7  
PO Box 5116  
Norwalk, CT 06856-5116

**Re: November 23, 2015 Exposure Draft of a Proposed Accounting Standards Update (ASU), *Business Combinations (Topic 805): Clarifying the Definition of a Business* [File Reference No. 2015-330]**

Dear Ms. Cospers:

The American Institute of CPAs (AICPA) is the world's largest member association representing the accounting profession, with more than 412,000 members in 144 countries, and a history of serving the public interest since 1887. One of the objectives that the Council of the AICPA established for the PCPS Executive Committee is to speak on behalf of local and regional firms and represent those firms' interests on professional issues in keeping with the public interest, primarily through the Technical Issues Committee (TIC). This communication is in accordance with that objective. These comments, however, do not necessarily reflect the positions of the AICPA.

TIC has reviewed the ED and is providing the following comments for your consideration.

### **GENERAL COMMENTS**

TIC is very supportive of the ED, which provides much improved guidance for the evaluation of the definition of a business. TIC favors an option for early implementation of the final standard (including adoption of the standard for applicable transactions in financial statements not yet issued) and requests a delayed effective date for mandatory adoption by nonpublic entities. TIC has also requested clarification of the Board's position on transition disclosures.

### **SPECIFIC COMMENTS**

*Question 1: Do you agree that to be a business a set of assets and activities must include, at a minimum, an input and a substantive process that together contribute to the ability to create outputs? If not, what other alternatives would you suggest?*

Yes, TIC agrees that an input and a substantive process for creating outputs are two necessary conditions to classify and account for a set of assets and activities as a business. TIC believes creating a minimum threshold will be helpful in reducing overly broad interpretations of the definition of a business that have occurred under extant standards.

*Question 2: Paragraphs 805-10-55-5A through 55-5D provide guidance on determining whether a set contains an input and a substantive process that together contribute to the ability to create outputs. Are the criteria appropriate, and would they be operable in practice? If not, why?*

Yes, TIC believes the criteria are appropriate and helpful to have in the guidance.

*Question 3: Would the proposed guidance be operable without the criteria in paragraphs 805-10-55-5A through 55-5D? Why or why not?*

TIC believes it is doubtful that the proposed guidance could be operable without the criteria in paragraphs 805-10-55-5A through 55-5D. As stated in the ED, these paragraphs provide a framework for evaluating whether a set of assets and activities includes both an input and a substantive process. The guidance relating to an acquired workforce is particularly important since it is a critical factor in the determination of a substantive process irrespective of whether the set has outputs. It is unlikely that preparers and practitioners could infer the Board's intentions, and TIC believes the outcome would be diversity in practice. Therefore, TIC strongly encourages the Board to retain paragraphs 805-10-55-5A through 55-5D.

*Question 4: Paragraph 805-10-55-9 provides that the presence of more than an insignificant amount of goodwill may be an indicator that an acquired process is substantive. Do you think this indicator is appropriate and operable? Why or why not?*

Yes, TIC believes the goodwill indicator in paragraph 805-10-55-9 is appropriate and operable. The components that comprise goodwill are often the indicators of a substantive process but not conclusively so. TIC agrees that the mere presence of more than an insignificant amount of goodwill is not conclusive that the set is a business. TIC also believes that preparers and practitioners will be able to exercise professional judgment to properly evaluate the presence of goodwill, along with other indicators, to determine whether an acquired process is substantive.

*Question 5: Do you agree with the changes proposed to the definition of outputs? That is, do you agree that for purposes of evaluating whether a transferred set is a business, outputs should be focused on goods and services provided to customers? If not, why?*

Yes. TIC believes the proposed changes to the definition of outputs make sense in light of new revenue standard.

*Question 6: Paragraphs 805-10-55-9A through 55-9C specify that if substantially all the fair value of the gross assets acquired is concentrated in a single identifiable asset, the set is not*

*a business. Is it appropriate to include such a threshold, and would it be operable? If not, why?*

Yes, TIC agrees that the proposed threshold is appropriate and that it would be operable, especially since paragraphs 805-10-55-9B through 55-9C provide additional application guidance that will be very helpful.

*Question 7: The threshold in paragraph 805-10-55-9A also applies to a group of similar identifiable assets. Would the identification of a group of similar identifiable assets be operable? If not, why?*

Generally, yes, the proposed threshold will be operable based on the additional guidance in paragraphs 805-10-55-9B and 9C.

*Question 8: Will the proposed guidance reduce the cost and complexity of applying the definition of a business? Why or why not?*

TIC believes the proposed guidance may have a neutral effect on cost and complexity when determining whether acquired assets meet the definition of a business. For many years, companies have been evaluating the definition of a business to determine whether assets acquired should be accounted for as a business combination or an asset acquisition. Under the proposal, an evaluation will still be necessary, but the criteria used in the evaluation will change. Unlike today, companies may no longer default to a conclusion that most acquisitions are business combinations, which frequently occurs under the existing definition of a business. As a result, TIC anticipates that more time may be needed to analyze transactions under the new definition and criteria.

Application of the new definition may also result in cost savings for some entities in the accounting for certain transactions. For example, if the definition of a business is applied less broadly as a result of the amendments in this ED, more acquired assets may meet the definition of an asset acquisition. If this is the case, implementation may be less costly since an asset acquisition tends to be less expensive and easier to implement than a business combination. Irrespective of the future impact on cost/complexity, TIC believes the amended standard will facilitate application of the definition of a business, reduce diversity in practice and improve financial reporting across multiple industries.

*Question 9: How much time would be necessary to adopt the amendments in this proposed Update? Should early adoption be permitted? Would the amount of time needed to apply the proposed amendments by entities other than public business entities be different from the amount of time needed by public business entities?*

As noted above, when applying the existing definition of a business to the analysis of acquired assets, many companies tend to default to business combination accounting. The proposed standard will require a more careful analysis of facts and circumstances, which may require more implementation time for those who have been applying the existing definition too broadly.

TIC believes that nonpublic entities may require a longer period of implementation to learn the new threshold and the related criteria. Nonpublic entities also tend to have fewer internal resources and less expertise on staff and will frequently look to their outside CPAs for assistance. TIC therefore recommends that nonpublic entities be given an extra year to implement the new standard.

TIC agrees that early adoption should be permitted.

*Question 10: Do you agree that the amendments in this proposed Update should be applied prospectively to any transaction that occurs on or after the date of adoption, and do you agree that there should be no explicit transition disclosure requirements? Why or why not?*

TIC believes prospective application makes sense but suggests that private entities be allowed to adopt the revised definition of a business for any transactions occurring in financial statements not yet issued. Most transactions involving acquisitions by private companies are not accounted for on a timely basis and may involve a 6-9 month lag. Public companies are more likely to be timely in accounting for these transactions.

As to transition disclosure, TIC was confused by the statement in paragraph BC45 that indicates the Board decided not to require any of the disclosures in paragraphs 250-10-50-1 through 50-3 of the *Accounting Standards Codification™ (ASC)*. TIC agrees that it's not necessary to quantify the impact of the accounting change on the income statement, but disagrees that all of the disclosures in paragraphs 250-10-50-1 through 50-3 should be omitted. Although most of these paragraphs apply only to disclosure of the quantitative effects of an accounting change and should not apply to this proposal, TIC questions why the Board would not require disclosure of the nature of and reason for the change in accounting principle as required by ASC 250-10-50-1a.

The suggested disclosure could be especially useful if the entity has similar purchase transactions in Year 1 and Year 2 of its comparative financial statements, and those transactions are accounted for differently as a result of the accounting change. For example, assume that real estate acquisitions with in-place leases occur in each of two years. Year 1 is accounted for as a business combination under existing GAAP, but Year 2 is accounted for as an asset acquisition under the proposed ASU. Financial statement users should be advised of the change through a qualitative disclosure.

TIC therefore suggests that the Board re-examine the statement made in the Basis for Conclusions and require the disclosures in ASC 250-10-50-1a.

*Question 11: Do the examples in paragraphs 805-10-55-51 through 55-88 clearly illustrate the application of the proposed guidance? Why or why not?*

Yes, the examples are clear and helpful.

*Question 12: Do the changes to the Master Glossary create any unintended consequences?*

No.

TIC appreciates the opportunity to present these comments on behalf of PCPS member firms. We would be pleased to discuss our comments with you at your convenience.

Sincerely,

A handwritten signature in black ink that reads "Michael A. Westervelt". The signature is written in a cursive style with a large initial 'M'.

Michael A. Westervelt, Chair  
PCPS Technical Issues Committee  
cc: PCPS Executive and Technical Issues Committees