On the Efficacy of "Acquisitions Method" Under FAS 141(R) in Reporting Business Combinations

This article provides an analysis of the current status and methodology of merger accounting in the United States. Taking up the issue from APB Opinion No. 16, this article critically evaluates the provisions of the various pronouncements on the subject viz. FAS 141 and 141(R). It highlights the points of upgradation introduced by FAS 141(R) over FAS 141 and discusses contentious and controversial issues emanating from FAS 141(R). Unresolved aspects of merger accounting are also enlisted. Read on…

Introduction

The policies and procedures of corporate management have undergone a complete metamorphosis in the preceding three decades. As the market efficiencies have approached perfection and trade boundaries have been belittled by technology, the world has dwindled to a shopping plaza. Competition has become unprecedentedly intense. Corporates are taking recourse to innovative business strategies to facilitate cost reductions, competitiveness and sustenance. Mergers, acquisitions and other forms of business combinations constitute cardinal ingredients of the "business strategy" toolbox. The incredible diversity of these corporate restructurings provides abundant business opportunities for the vigilant and diligent entrepreneur. Consequently, the frequency of such "business combinations" has grown manifold in the recent past. Furthermore, these restructurings have become immensely complex with the evolution of commercial wisdom. It is therefore imperative that, accounting regulators worldwide get together to formalise rational and streamlined standards in the context of "business combinations accounting" to facilitate undistorted dissemination of information to the relevant stakeholders. It needs to be emphasised here that the extant standards in this regard are inconsistent, not only across different types of business combinations but also across different countries.

Prof. J. P. Singh
(The author may be reached at jpsiitr@gmail.com.)

It may be noted that FAS 141(R) has been substantively adapted into the Accounting Standard Code (ASC) promulgated by the United States Financial Accounting Standards Board (FASB) as ASC No. 805. This ASC of the FASB constitutes the complete source of extant authoritative generally accepted accounting principles (GAAP) recognised by the FASB to be applied to non-governmental entities. The ASC is effective for interim and annual periods ending after September 15, 2009. It has been formulated through a comprehensive restructuring and reorganising of the various pronouncements of the FASB from time to time and now, constitutes the sole authoritative diktat of the FASB on the US GAAP superseding all the erstwhile accounting standards. All accounting literature not explicitly included in *the ASC has been declared to be non-authoritative by the FASB.*

The Backdrop

As one of the most sensitised professional accounting outfits, the United States accounting regulators took a lead in this regard, with the Accounting Principles Board (APB) Opinion No. 16, *Business Combinations*, being issued in 1970. The said opinion enabled accounting for business combinations using either of two methods of merger accounting *viz.* (i) the pooling method and (ii) the purchase method. However, an acquiring company had to satisfy no fewer than twelve criteria in order to qualify for using the pooling method. The default was the purchase method.

The pooling method was beset with controversies from the very outset. Under this method, a business combination was accounted for at book value. An exchange of equity interests enabled the acquisition/ transfer of control. In effect, this amounted to, simply, an aggregation of the book values of the corresponding constituent accounts of the two merging companies. The difference between the book value of the stock exchanged and the net assets acquired was recognised to equity accounts. No other assets or liabilities were recognised. The *lacunae* in the pooling method are not hard to find. The fact that assets were taken at book values and, consequently, intangibles were either totally ignored in the post merger balance sheet or were incorporated therein at gross undervaluation implied that prospective return on investment got unrealistically exaggerated not only through a shrunk asset base, but also due to inflated profits on account of under-amortisation of intangibles to the income statement. In view of the aforesaid, it was but natural that most entrepreneurs and corporates made the most of the leeway provided by the accounting mandates and adopted the pooling method for the reporting of business combinations. This enabled an escape route from the revaluation of accounts on acquisition to their respective fair values and the recording of intangibles like goodwill, brand names, *etc.* into the books of accounts of the acquirer, post acquisition.

There were several indirect implications as well *viz.* post merger sale of assets that were acquired in course of merger and recorded at book values, resulted in the reporting of accounting profits that would not have been so reported, had the assets been recorded at their respective fair values on merger. Distribution of these profits tantamounted to withdrawal of capital, adversely affecting the interests of creditors. Additionally, the adoption of varied accounting methods for reporting of transactions that were, in essence, economically similar, rendered the post merger performance incomparable and difficult to assess with consistency. This went against the interests of the general investing public as well as the accounting regulators.

The US Financial Accounting Standards Board (FASB hereinafter) took cognizance of these issues and, in August 1996, initiated the process for enhancing transparency in the accounting and reporting of business combinations and the related intangibles by assigning this mandate to the Emerging Issues Task Force (EITF hereinafter). The EITF found that the twelve criteria that enabled the discretion to use the pooling method were ineffective in segregating economically dissimilar transactions in the context of business combinations. Consequently, such economically dissimilar business combinations were being accounted for and reported homogeneously, and conversely, economically similar business combinations that fell in the divide of these twelve criteria were being done so heterogeneously, thereby violating representational faithfulness and comparability. It was also argued that entities that could not meet the said twelve criteria faced competition on account of purely illusory, non-economic and law-wrangling factors for potential acquisitions with entities that did meet the stipulated criteria and thereby could apply the pooling method.

FAS 141, Business Combinations (FASB, 2001)

Based on the EITF's recommendations, the FASB issued Financial Accounting Standard (FAS hereinafter) 141, *Business Combinations*, in June 2001, made effective for all business combinations initiated after June 30, 2001. FAS 141 explicitly mandated the use of only the purchase method to account for and report business combinations. Almost simultaneously, FAS 142, *Goodwill and Other Intangible Assets*, was released in June 2001. It was made effective from January 31, 2002. FAS 142 categorised intangible assets into two classes viz. those with (i) finite and (ii) indefinite useful lives. The latter category of assets was not required to be amortised. Nevertheless, they were to be tested for impairment at least annually. The assets with finite lives were to be amortised over the useful life, as earlier. Since acquired goodwill was in the non-

FAS 141 received a mixed response from industry with the primary criticism being the modus operandi for goodwill computations. The said standard did not lay out any explicit methodology for arriving at the intrinsic value of goodwill to the acquirer. Rather, it simply treated goodwill as a residual asset created in the acquisition process by defining it as the excess of the price paid over the net assets acquired.

amortisation category, one of the motivations for use of the pooling method viz. lesser charge to the income statement on amortisation was neutralised as part of the FAS 141-142 scheme of things. The reluctance of companies to allocate part of purchase price to goodwill was, thus, addressed (Uzma, 2009, pp. 19-27). Additionally, FAS 141 attended to minor implementation issues in relation to the purchase method as well. Unlike the provisions of Opinion 16 that mandated recognition of intangible assets separate from goodwill that could be *identified or named*, FAS 141 prescribed recognition of intangible assets as assets apart from goodwill that met either the *contractual–legal or the separability* criterion. Furthermore, FAS 141 also required additional disclosure over and above the requirements of Opinion 16 of the primary reasons for a business combination. Besides, the allocation of the purchase price paid to the assets acquired and liabilities assumed was also to be disclosed.

FAS 141 received a mixed response from industry with the primary criticism being the modus operandi for goodwill computations. The said standard did not lay out any explicit methodology for arriving at the intrinsic value of goodwill to the acquirer. Rather, it simply treated goodwill as a residual asset created in the acquisition process by defining it as the excess of the price paid over the net assets acquired. It follows that the recorded value of goodwill may fail to reflect the full economic value of the said asset to the acquirer (Miller, Bahnson, & McAllister, 2008, pp. 34-39).

Another concern voiced by stakeholders was the revised criterion for according recognition to intangible assets. FAS 141 provided that only those intangible assets be individually and explicitly recognised that satisfy either contractual-legal criterion or the separability criterion. Intangibles not satisfying either of these would be part of the residual class (goodwill). FAS 141 also prescribed explicit valuation, in relation to each of the company's reporting units or business segments, of such intangibles that figure in a list specifically provided in the standard. It was widely perceived that the criterion prescribed for identification of separate intangibles was too stringent, particularly so, in case the intangible failed to feature in the relevant list.

Additionally, several grey areas were observed in FAS 141, for example (i) limited realm of applicability, it being confined to business combinations wherein control relocation was attained only by a *transfer of consideration*; (ii) absence of a structured methodology for the measurement of non-controlling/minority interest's share in the subsidiary, upon consolidation of accounts; (iii) lack of precise prescriptions for assignment of asset values to relevant reporting units of a company; (iv) want of unambiguous tests for ascertaining the useful life, finite or indefinite, of intangibles (Quick and Goldschmid, 2002, pp. 61-63; Lewis, Lippitt, & Mastracchio, 2001, pp. 26-30).

Several other inconsistencies subsisted in FAS 141 in relation to accounting for acquisition related costs, in process R&D, bargain purchase and negative goodwill, step acquisitions, contingent considerations, *etc.* There were instances when assets and liabilities were required/allowed explicitly or impliedly to be recorded on dates other than the acquisition dates or at values that were different from their respective fair values on the acquisition dates. Issues of non-harmonisation with the corresponding international standards for furthering the program of global convergence were also observed in FAS 141.

It was, therefore, not surprising that, in 2002, the EITF of the FASB started fresh deliberations on business combinations. The efforts of the EITF culminated in the issue of the revised FAS 141 i.e. FAS 141(R) by the FASB that addressed several of the inconsistencies of FAS 141. FAS 141(R) was made applicable with effect from December 15, 2008.

FAS 141 Revised, Business Combinations (FASB, 2007)

FAS 141(R) reflects a paradigm shift in the conceptual underpinnings of accounting for business combinations in the sense that it defines the reporting entity as the entire economic enterprise created by the combination. As such, the consolidated balance sheet is required to present a reporting of the entire set of acquired assets and assumed liabilities including the minority (non-controlling) interests.

Such interests shall be merged with the stockholders' equity in reporting and reported neither as a liability nor as a mezzanine item not specifically classified as liability or equity. Besides this, the cash flow and equity statements shall also be restructured in a manner to present the whole enterprise, post acquisition, enabling an explicit evaluation of the content and role of holding company's management. The income statement will, similarly, present results for the entire enterprise. However, the said statement shall include a schedule that splits the bottomline into and reports components attributable to the controlling and non-controlling interests with the earnings per share data being computed and presented only with reference to the income related to controlling interest shareholders. Secondly, the push towards upstaging fair value based reporting is given a further impetus in FAS 141(R) (Singh, 2011, pp. 113-126; Walsh, 2006, pp. 2-3).

FAS 141(R) also provides extended accounting and practical directives in implementing the purchase method (renamed as "acquisition" method) over FAS 141, on several issues that include: the recognition and measurement of the assets acquired and liabilities assumed, controlling and non-controlling equity interests, goodwill acquired, gains from bargain purchase options, *etc.* in addition to rationalising the disclosure requirements.

A summary of the salient upgradations introduced by FAS 141(R) over its predecessor seems to be in order at this point.

(a) What Constitutes a "Business"?

As mentioned above, FAS 141 applies only to the limited set of business combinations that involved transfer of interests pursuant to *movement of consideration*. Thus, mutual entities combining together without any transfer of consideration did not attract FAS 141. However, FAS 141(R) has broadened the scope of applicability of the acquisition method by defining an "acquirer" as an entity that *obtains control of the other business*. The restriction on the scope of applicability of FAS 141 caused by requiring *movement of consideration* is, now, removed. Thus, business combinations would need to be recorded and reported by the acquisition method irrespective of the fact whether the transfer of interests is caused through a transfer of consideration or otherwise. However, in the latter case, the estimated fair values may be dubious (Davis & Largay, 2008, pp. 26-31).

(b) Treatment of Acquisition Costs

Acquisition costs are those costs that are incurred, directly or indirectly, in relation to identification of potential acquisition targets, collecting and analysing data, arranging funds for the acquisition or such similar activities. FAS 141 allowed these costs to be aggregated with the purchase price, thereby increasing the amount of goodwill. The entire goodwill was subjected to impairment testing as prescribed by FAS 142. This treatment was strongly contended on the premise that such costs do not result in any value addition to acquired assets and, as such, should neither be classified as assets in their own right nor aggregated with goodwill. Accepting the argument, FAS 141(R), now requires these costs to be expensed forthwith. The opposing school contends that (i) the expensing of these costs is inconsistent with the standard accounting practice in respect of costs of similar nature that are incurred in new project implementation, example, capitalization of preoperative costs and (ii) such costs are given due weight in formulating a purchase price and, as such, these costs should form part of investment and should not be expensed (Davis & Largay, 2008, pp. 26-31).

(c) Treatment of In-Process R & D Costs

There may be instances in which the acquired company was carrying out research and development activities that, although yet to be completed, seemed to have high potential on the date of acquisition. As part of the scheme of transfer, the acquirer may get the right to carry forward the R & D program to, probably, a positive, commercially viable and profitable proposition.

FAS 141 read with FAS 142 required acquirers to perform appropriate valuation of in-process R & D assets for the purpose of accounting for the acquisition. Such expenses were, then, to be written off forthwith to the income statement (Miller, Bahnson, and McAllister, 2008, pp. 34-39). In the event that such assets were significant and had substantively influenced the acquisition decision,

FAS 141(R) has radically revised the treatment of in-process R&D costs by requiring that such costs be measured at fair value. They may, then, be capitalised with the provision of annual impairment testing to ensure that any decline in value is immediately taken cognizance of.

the balance sheet would be missing out on such important reporting. By the same logic, the income statement would also be distorted by the writeoffs of such assets (Smith & Saemann, 2007, pp. 16-21).

FAS 141(R) has radically revised the treatment of in-process R&D costs by requiring that such costs be measured at fair value. They may, then, be capitalised with the provision of annual impairment testing to ensure that any decline in value is immediately taken cognizance of. For this purpose, they shall be classified as assets with indefinite life until the project is either completed or abandoned. Importantly, these in-process R & D costs are to be identified independently and their implied value not grouped in goodwill. It needs to be emphasised here that R&D not obtained through an acquisition is treated quite differently (Desroches, 2007). The eagerness of FASB to usher in fair value accounting is clearly manifest in these provisions. The FASB also believes that the provisions of FAS 141(R) will ensure that spurious losses do not enter the income statements and the balance sheets will be more complete and the overall accounting process more transparent.

(d) Treatment of Goodwill

Goodwill, in essence, represents the excess consideration paid by the acquirer over the fair value of net assets acquired in a business combination. The issue that remains unsettled is whether such excess payment was justified i.e. whether the excess payment represents the fair value of a real asset or whether it was merely an error of judgment. FAS 141 prescribed that the excess of the consideration paid over the aggregated fair value of the acquirer's proportionate share of acquired identifiable net assets be recorded as goodwill. No goodwill was to be attributed to the non-controlling interests. The basic shortcoming of this method is that it does not intrinsically/explicitly measure goodwill; it simply treats goodwill as a residual class wherein any surplus is to be credited.

While retaining the residual cost as a measure of goodwill, FAS 141(R), prescribes its computation as GW=(CT)+(NC)-(NAL) where CT is the consideration transferred by the acquirer to the acquiree, NC is the fair value of any non-controlling interest and NAL is the algebraic aggregate of the fair values of the identifiable assets acquired and liabilities assumed by the acquirer on the acquisition date (FASB, 2007, p. iv). Implicitly, therefore, under FAS 141(R), the measurement of the entire non-controlling interest must be at fair value on the acquisition date. It may be noted that this is clearly in distinction of the corresponding provision of IFRS 3 that enables the measurement of non-controlling interest not at the full fair value but at its proportionate share of the identifiable net assets (Graziano & Heffes, 2008, pp. 34-41).

FAS 141 prescribed that the excess of the consideration paid over the aggregated fair value of the acquirer's proportionate share of acquired identifiable net assets be recorded as goodwill. No goodwill was to be attributed to the non-controlling interests. The basic shortcoming of this method is that it does not intrinsically/explicitly measure goodwill; it simply treats goodwill as a residual class wherein any surplus is to be credited.

However, FAS 141(R) does require separate valuation and accounting of acquisition costs, R&D, and contingencies thereby reducing the goodwill residual.

(e) Bargain Purchase Transactions

A bargain purchase acquisition is an acquisition deal wherein the aggregate of (i) the consideration transferred and (ii) fair value of any non-controlling interest in the acquiree on the date of acquisition is less than total fair value (on the date of acquisition) of the identifiable net assets acquired (FASB, 2007, p. iv). The provisions of FAS 141 mandated that the negative goodwill, emanating as above, was to be proportionately reduced from the book value of certain assets. Surplus, if any, remaining after such apportionment was to be recognised as an extraordinary gain. However, this treatment implied that the recording of such assets that were involved in the apportionment were no longer reported in the books at fair value. Further, there was arbitrariness manifest in the distribution of such negative goodwill. This under-reporting of assets available to management for earning returns led to distorted measurement of returns on investment. In addition, management's successful negotiation was not highlighted (Ketz, 2005, pp. 47-50).

On the other hand, FAS 141(R) requires that companies record this excess value received as a gain on the income statement (net of deferred taxes). Thus, the assets acquired continue to remain at fair market value. Nevertheless, these provisions met with strong dissent on the premise that fictitious or manipulative gains could enter the income statement emanating from deliberate and/or premeditated inaccuracies in the estimation of the relevant fair values or even the use of measures that, although permitted by statute, do not represent fair values (Silliman, 2008, pp. 32-36).

(f) Contingent Considerations

Sometimes, as part of negotiation of acquisition deals, the parties thereto agree to contingent consideration arrangements. In such cases, the parties agree to a further transfer of funds, depending on future events. Most of these types of contingent considerations were not included in the scheme of FAS 141 for determining the recorded price. However, subsequently, if and when (i) earnings-target related additional payments were made, goodwill was to be enhanced by like amount; (ii) stock price related payments were made, such payments were to be transferred to paid-in capital and (iii) conversely, the goodwill or the paid-in capital, as the case may be, was to be reduced in the event that refunds were received. It was argued that FAS 141 prescribed procedures reduced the managers' accountability (Miller, Bagnson, and McAllister, 2008, pp. 34-39). Further, the financial statements so produced were uninformative of the future liabilities relating to the acquisition.

On the other hand, the valuation of these contingent considerations at their estimated fair value on the date of acquisition is now mandated by FAS 141(R). These contingent considerations are then to be recorded as assets and liabilities on acquisition. Furthermore, until the resolution of these contingencies, marking to market of their valuations is required. All changes in value due to the marking to market are to be carried to the income statement. The difference between the amount received or paid on settlement less the carrying value shall constitute the gain/loss on settlement. The income statement of the relevant period shall carry the gain or loss on settlement. If contingent consideration relates to shares, the difference between the initial fair value and final fair value is to be recorded in paid-in capital.

(g) Other Contingencies

There are, usually, some contingent assets and liabilities acquired as part of a business combination. FAS 5 deals with the accounting and reporting of such accounts on the consolidated entity's financial statements. It provides, in essence, that (i) gain contingencies are never to be recognised; (ii) loss contingencies that are deemed probable and reasonably estimable are to be recorded and reported; (iii) other loss contingencies are to be disclosed or ignored. Obviously, the non-inclusion of these acquired contingent assets and liabilities renders the statements incomplete. Such omissions distort the actual cost of acquisition and the amount of goodwill. Also, the users of such statements are uninformed about possible future outcomes of these contingencies.

FAS 141(R) supersedes the treatment prescribed under FAS 5 by providing explicit directives in respect of several types of contingencies and exempting them from FAS 5. FAS 141(R) provides inter alia that (i) all contractual contingent assets and liabilities be recorded at estimated fair values on the acquisition date and reported as such by the acquirer; (ii) if it is more likely than not that an asset or liability exists under the elements definition in Concepts Statement 6, in relation to other contingencies, such contingencies be also recorded at estimated fair values. Further, such contingencies are to be remeasured conservatively until they are finally settled. Thus, contingent assets (liabilities) are to be valued at the lower (higher) of their original or later value.

(h) Step Acquisitions

"Step acquisitions" relate to those instances where the acquirers acquire the controlling stake in small bits and pieces i.e. the acquisitions are achieved in small steps. FAS 141 provided that the original book value of each investment in the series that are culminated in control, be preserved. Such book value may have been cost, market value, or equity method balance. Once control was achieved, the book value of each purchase was used to calculate the total consideration. Thus, the total consideration may not have been the same as aggregate fair value of the total acquisition at the acquisition date. Thus, FAS 141 led to a valuation that was a cost-based measure which was not reflective of the fair value of gaining control. This was so because the cost based value of the holdings included costs of acquisitions made at different points in time and hence, in different market conditions. In times of escalating prices, this could short-value the consideration of gaining control and thus, understate value of goodwill than its fair value. Not only this, there could have been situations in which the actual (not fair) value of this consideration was less than the fair value of net assets' acquired. This would imply that these assets be booked at below their intrinsic value (Wendell, 2008).

FAS 141(R) recognises this flaw in FAS 141. It, therefore, requires that, on achieving control, adjustment to fair value must be made for each block of investment. The differentials emanating from such adjustments are to be transferred to the income statement for the present period. This follows from the fact that FASB acknowledges that the character of the investment undergoes a significant modification due to alteration from a non-controlling interest to a controlling interest. FAS 141(R), accordingly, stipulates a revision in the classification and measurement of the investment (FASB, 2007, p. 384). The recognition of a gain/loss in the case of step acquisitions is simply a deferred recognition, when control is achieved, of fair value that was not reported due to the valuations of blocks of investments on the basis of historical cost (FASB, 2007, p. 387).

It was contended before the FASB that the other *comprehensive income* and not the current income statement should reflect the adjustments due to bringing up the step acquisitions to fair value since unrealised gains/losses related adjustments on available-for-sale securities were carried that way (Davis and Largay, 2008, pp. 26-31). FASB, however, felt that, in step acquisitions, *derecognition of the investment asset* by the acquirer in its consolidated financial statements takes place when it achieves control. Now, *when the securities are derecognised*, changes in the value of available-for-sale securities are recognised not to *other comprehensive income* but to net income (FASB, 2007, p. 389).

(h) Measurement Period

It can very often happen that acquirers are unable to estimate the fair values of all the assets acquired and liabilities assumed at the acquisition date. In such situations, FAS 141 allowed the acquirers the leeway to assign provisional values up through the first accounting period date after the acquisition. Thus, these values were allowed to be adjusted for upto a year, post acquisition. FAS 141 did not explicitly mandate any particular outlet for these adjustments i.e. whether they be charged off to current income or applied retrospectively to equity. This ambiguity led not only to inconsistencies in practices but also made the statements less reliable insofar as the combination statistics on the acquisition date were concerned.

FAS 141(R) explicitly allows the acquirer a period of upto one year to crystallise the fair values of the assets acquired and liabilities assumed as on the acquisition date. Further, any adjustments in the provisional values are required to be reported in such a manner as if the revised amounts had been known on the acquisition date.

Merger Accounting: The Road Ahead

The present status of accounting and reporting for business combinations, as symbolised by FAS 141(R), has been elucidated above substantively. The reactions to the Exposure Draft of FAS 141(R) were profound with several interest groups being skeptical of the, then proposed, changes on the premises that such changes would neither increase transparency in reporting nor enhance its reliability and comparability, while adding to the complexity of the statements, thereby making them difficult to decipher for the layman investor (Chavern, 2005). Responses to the FASB Exposure Draft also indicated that the FASB was already seized with projects on the conceptual framework. Accordingly, the related changes in FAS 141(R) were premature and unwarranted. It was also opined that in its eagerness to usher in fair value accounting, the FASB, was occasionally sidetracking the concepts of comparability and conservatism, in the process of formulating the standards. As is apparent, a business combination is now required to be reported at full fair value. This makes the reporting less reliable, although, admittedly, it is more relevant and transparent. The costs associated with the reporting and audit exercise, nevertheless, escalate.

One of the most contentious provisions in FAS 141(R) is the change in the philosophy underlying the accounting for business combinations from the parent theory to the full economic-unit theory. Convergence with the IAS was not reached on this issue. FAS 141(R) requires the measurement

FAS 141(R) explicitly allows the acquirer a period of upto one year to crystallise the fair values of the assets acquired and liabilities assumed as on the acquisition date. Further, any adjustments in the provisional values are required to be reported in such a manner as if the revised amounts had been known on the acquisition date.

yardstick of fair value for non-controlling interests, whereas the corresponding IAS allows the discretion to use either proportionate interest in the identifiable assets or fair value for the measurement of such interests. Some respondents vehemently argued that, in cases where less than 100% of an acquiree is obtained, to gross up goodwill and non-controlling interests is clearly inappropriate (Teixeira, 2005). Their contention was that only the parent should be attributed goodwill as it is defined as a residual. Particularly in cases where less than 100% is acquired, non-controlling interest should not be attributed any goodwill. Doing so could overstate the entity's true value. It was also argued that stockholder's equity should not include non-controlling interest. The non-controlling interest does not represent the true equity of the company (Teixeira, 2005).

Provisions of FAS 141(R) on the treatment of contingencies also generated a furor. In context of these provisions, concerns were voiced on the issue of ascribing reportable values to such contingencies or contingency considerations. Since, contingencies are intrinsically probabilistic and conditional and without any live markets to facilitate fair value estimation, reliable estimation of value is a serious challenge (Singh, 2015, pp. 59-69). Besides, such valuations may destroy the confidence of the end users of the financial statements in the reports. Not only this, such valuation needs to be a perpetual exercise until the contingency is settled since a continuous marking to market is also stipulated by FAS 141(R). Opportunities for manipulation by the management are also upstaged. Companies could also manipulate operating performance by distorting the value of contingent considerations (Graziano & Heffes, 2008, pp. 34-41; Price Waterhouse Coopers, 2007).

The treatment of in-process R & D costs under FAS 141(R) (that requires such costs to be accounted for at fair value, recorded as an intangible asset in the consolidated statements and then tested for impairment on a regular basis) is inconsistent with FAS 2 that relates to accounting for other in-process R & D. FAS 2 requires all other in-process R&D to be expensed. However, FAS 2 and FAS 142 respectively will continue to govern future investments in R&D following the acquisition date. Here lies the source of another anomaly. The acquired in-process R&D has value (FAS 141(R)), whereas future additions to the acquired in-process R&D as well as internally developed in-process R&D do not have value. It is emphasised that the method for reporting should be independent of the manner of acquisition of the asset.

There is also some divergence between FAS 141(R) and the corresponding IAS 38. Although treatment of acquired in-process R&D is identical, non-acquired in-process R&D is treated differently under the two standards. As per IAS 38, (i) expenditures relating to the research portion of a project are to be forthwith expensed as incurred, with no recognition as an intangible asset; (ii) expenditures on developmental activities may be recognised as intangible assets (Andrews, 2009, pp. 125-136).

Conclusions

There is no debating the fact that, through the issuance of FAS 141(R), substantial progress has been achieved by the FASB in upgrading the quality, relevance and representational faithfulness of financial reporting for business combinations. However, a study of the responses received to the Exposure Draft equally unequivocally testifies that issues subsist wherein divergence of opinion is strong. In particular, it is, now, opportune to undertake an analysis of feedback from stakeholders accompanied by a fresh and extended review of example (i) the traditional parent vs. the revolutionary economic-unit view of the post-acquisition entity; (ii) the principles and methodology governing recognition and measurement of contingencies; (iii) treatment of contingencies consideration; (iv) the accounting and reporting of R&D activities. The cost aspect associated with the compliance of FAS 141(R) needs also to be assessed.

Besides, the issue of harmonisation between the standards issued by FASB and International Accounting Standards Board (IASB, 2008) is still quite distant. This is despite the fact that FAS 141(R) was a cooperative project between the FASB and IASB. As mentioned above, some instances of divergence include *modus operandi* for valuation of non-controlling interest, measurement and reporting of contingency considerations, and valuation and treatment of assets and liabilities arising from contingencies. Some of the differences between FASB and IASB standards were allowed on the necessity of these standards to be consistent with other standards of the same authority. Furthermore, it was also felt that most of these differences would be addressed as part of current or future joint projects of the FASB and the IASB (FASB, 2007, p. 333). ■