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FAS 141R NOW EFFECTIVE: Impact of New Accounting Rules For Business Combinations Should be Considered in Acquisition Planning

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In late 2007, the Financial Accounting Standards Board (FASB) issued revised guidance on accounting for acquisitions under Statement of Financial Accounting Standards No. 141R *(Business Combinations)*. FAS 141R has now become effective for annual periods beginning after December 15, 2008 and will apply to all transactions within the rule's definition of a "business combination" where an acquirer obtains control of one or more businesses.

A detailed overview of FAS 141R is beyond the scope of this newsletter and companies should discuss the impact of the rule with their accounting advisors and be cognizant of the impact of the new rule on pending and potential acquisitions. Generally speaking, however, the new rule is seen as capturing a wider group of acquisition transactions than were subject to the prior purchase method rule due to the new definitions of "business" and "business combination." The rule expands the use of "fair value" (as of the date that control is obtained) as the relevant accounting measure for assets acquired and liabilities assumed and requires more disclosure to reflect the nature and financial effect of the business combination.

In addition, FAS 141R requires the acquirer to recognize goodwill as of the acquisition date, measured as a residual amount in excess of the fair values of the identifiable net assets acquired and also alters, among other things, the accounting of earn-outs and treatment of transaction expenses. Specifically, earn-outs will be required to be

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recorded at fair value on the acquisition date, rather than permitting the recognition of earn-outs to be delayed until payment is reasonably assured. Furthermore, transaction expenses such as fees paid to investment banks, attorneys, and valuation experts are no longer included in goodwill and capitalized as in the past. Rather, such amounts will be required to be expensed as incurred against net income. This new expense recognition rule may cause some indirect disclosure or rumors of possible acquisition activity as close readers of financial statements see a "spike" in such expenses prior to disclosure of a transaction.

The stated objective of FAS 141R is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial reports about a business combination, and to further align U.S. accounting practices more closely with international financial reporting standards. However, the full impact of the rule change will take time to understand and transitional problems may occur as parties become familiar with the rule and its impact on deal structures.

Understanding the impact of FAS 141R will be a critical component of a company's acquisition strategy, execution, and reporting processes. Companies should assess and discuss the new rule in detail with its accounting advisors, including both how the acquisition and the related acquisition expenses will be treated. From an acquisition process perspective, companies with an active acquisition strategy should ensure they have reviewed and updated their strategy against the new rule, and, on an on-going basis, structure new acquisition proposals having reviewed the accounting impact of the deal terms under this new rule.

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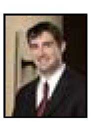

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