



**Request for Additional Comments on the Exposure Draft,  
*Not-for-Profit Organizations: Mergers and Acquisitions*  
Comment Letter Summary  
(As of August 12, 2008)**

**OVERVIEW**

1. The Board's October 2006 Exposure Draft, *Not-for-Profit Organizations: Mergers and Acquisitions*, proposed that mergers not be distinguished from acquisitions. At that time, the Board noted that combinations (mergers and acquisitions) are generally acquisitions and because those that are not acquisitions cannot be distinguished using an unambiguous basis, all mergers and acquisitions by not-for-profit organizations should be accounted for using the acquisition method. However, most respondents, including participants in a March 2007 roundtable, said that mergers among not-for-profit organizations occur with greater frequency than they do among business entities, and most of those respondents also argued that mergers can and should be distinguished from acquisitions. For a fuller discussion of the comments received on this issue, see paragraphs 3 and 6–21 of the comment letter summary on the responses received for the Exposure Draft, which is posted at the [FASB's project website](#). Individual respondent's comment letters also are available at the [FASB's website](#).
2. At its September 19, 2007 meeting, the Board reconsidered its earlier tentative conclusion and tentatively decided to revise its proposed Statement. On May 9, 2008, the FASB issued a paper seeking additional comments on the appropriateness and workability of potential criteria for distinguishing a merger of two or more not-for-profit organizations from an acquisition by a not-for-profit organization. Sixteen constituents responded to that [Request for Additional Comments](#) (Request), and raised several specific issues. This summary provides an overview and summary of respondents' comments and suggestions for those issues.

## Respondent Profile

3. Exhibit A, at the end of this summary, provides a list of the 16 respondents. Their comment letters are available at the [FASB's website](#).
4. The following table summarizes the types of respondents.

<b>Number and Type of Respondents (by Occupation/Role)</b>	
<b>Type of Respondent</b>	<b>Number</b>
<b>Public Accounting</b>	
Big Four Accounting Firm	3
Other Accounting Firm	2
<b>Total Public Accounting</b>	<b>5</b>
<b>Professional Organization</b>	
CPA Society	3
AICPA Committees	2
<b>Total Professional Org.</b>	<b>5</b>
<b>NFP Preparer</b>	
Social Service Organization	2
Religious	1
<b>Total Preparer</b>	<b>3</b>
<b>Individuals</b>	
Academic	1
Other	2
<b>Total Individual</b>	<b>3</b>
<b>Total Respondents</b>	<b>16</b>

## Overall Position

5. Fifteen of the 16 respondents generally support the Board's proposal to distinguish a merger of two or more not-for-profit organizations (or not-for-profit activities) from an acquisition by a not-for-profit organization. One respondent did not express a discernable position on any of the issues raised. The rest of this summary examines the remaining 15 comment letters.
6. Most respondents also agree that the proposed criterion for distinguishing a not-for-profit merger from an acquisition, namely that the governing bodies of two or more not-for-profit organizations cede control of those organizations to create a new organization, is appropriate and necessary. However, only one respondent suggested that such a criterion is sufficient to stand alone. A few respondents noted that

additional criteria are needed to more effectively convey the merger definition. Most others suggested that, instead of additional criteria, the final Statement include guidance in the form of examples, indicators, or both of ceding of control to make the guidance more operational and workable in practice. Lastly, three respondents suggested the Board make substantive revisions to the definition of a merger. Two of those respondents suggested a different underlying principle upon which the definition could be based: one suggested broadening the definition to include *distressed mergers* and the other suggested that a *public service concept* is integral to defining a not-for-profit merger. The following table summarizes those positions by types of respondents:

<b>The merger definition...</b>					
	<b>Total</b>	<b>Public Accounting</b>	<b>Professional Organization</b>	<b>NFP Preparer</b>	<b>Individuals</b>
Is sufficient	1		1		
Needs additional criteria	2	1		1	
Needs additional criteria and guidance	1		1		
Needs additional guidance	8	4	2	1	1
Needs substantive revision or clarification	3		1	1	1
<b>Total Respondents</b>	<b>15</b>	<b>5</b>	<b>5</b>	<b>3</b>	<b>2</b>

7. Some respondents also provided specific comments that offer some insights about the frequency with which mergers are occurring among not-for-profit organizations. For example, both the United Way of America (CL #7) and Girl Scouts of the USA (CL #14) are actively encouraging local United Ways and Girl Scout councils to consider merger opportunities. Similarly, the Board has become aware of donors (foundations) that are actively encouraging the organizations they support to consider opportunities to improve their financial health and better align their resources and missions for greater social impact. They are recommending strategies such as restructuring, repositioning, and reinvention, which are sparking interest in opportunities for mergers among not-for-profit organizations ([www.tbf.org/UnderstandingBoston](http://www.tbf.org/UnderstandingBoston)). Girl Scouts of the USA noted that it is “in the midst of a three-year realignment” that will take the Girl Scouts from 312 to 109 councils as the result of 80 mergers among various independently incorporated councils.
8. Lastly, some of the respondents who agree that the standards for financial reporting can and should distinguish between a merger of not-for-profit organizations used this opportunity to also remind the Board of their earlier comments made in response to the Exposure Draft. For example, Deloitte (CL #6) noted that although the Board plans to move forward with the proposed carry-over basis of accounting for mergers, it maintains that fresh-start accounting would provide financial statement users with the most relevant information. Similarly, BDO Seidman (CL #13) said “while we recommended fresh start accounting, rather than carryover basis, for mergers, we understand and do not object to the Board’s pragmatic decision to use carryover basis.”

## ISSUE SUMMARY

9. The Request asked specific questions that collectively sought comments on the appropriateness and workability of potential criteria for distinguishing a merger from an acquisition. The majority of respondents addressed most of the issues raised, but some addressed only a few specific issues. The following paragraphs summarize respondents' comments for the issues raised:
  - a. Definition of a Merger and Distinguishing among Combinations (paragraphs 10–19)
  - b. Exclusion of Joint Ventures from the Scope of the Final Statement (paragraphs 20–23)
  - c. Additional Criteria and Guidance (paragraphs 24–28)
  - d. Opt-Out Clauses (paragraphs 29–32).

In addition to the feedback received from respondents to the Request, during July and August the FASB conducted five field visits with senior executives and managers and external auditors of organizations involved in combinations of not-for-profit organizations. The purpose of the field visits was to test the workability of the proposed guidance when applied to five specific “real-world” transactions. The FASB thanks the participating organizations for their time and input.

### **Issues 1 and 2: Definition of a Merger and Distinguishing among Combinations**

10. Question 1 of the Request asked respondents whether the definition of a merger is appropriate for distinguishing mergers from acquisitions by not-for-profit organizations. The Request noted that the feature that distinguishes a merger from an acquisition (by purchase or gift) is that “the governing bodies of two or more not-for-profit organizations cede control of those organizations to create a new organization” (paragraph 7). In contrast, it noted that in an acquisition, “one organization obtains control over the net assets of another organization, business, or not-for-profit activity by purchase, gift, or otherwise” (paragraph 7).
11. Question 2 of the Request asked respondents whether the definition of a merger (quoted in the prior paragraph), together with the definition of control, is workable in practice—namely, whether or not the definition can be applied with a reasonable degree of consistency, especially when distinguishing a merger from an acquisition

and a joint venture. The Request defined *control* in the same manner as paragraph 20 of AICPA Statement of Position 94-3, *Reporting of Related Entities by Not-for-Profit Organizations*, and paragraph 11.08 of AICPA Audit And Accounting Guide, *Health Care Organizations*: the direct or indirect ability to determine the direction of management and policies through ownership, contract, or otherwise.

12. Most respondents agree that the definition of a merger, together with the definition of control, is appropriate for distinguishing mergers from acquisitions. However, respondents suggested that the Board clarify the definitions by adding language that more clearly communicates the Board's intent regarding the types of combinations that are within the scope of the proposed Statement and those that are not.
13. With respect to the definition of a merger, several of the requested clarifications would emphasize, either within the definition of a merger or by using an additional criterion, that the combination must be of a permanent nature and not temporary [Teresa Gordon (CL #2), Grant Thornton (CL #10), Florida Institute of CPAs (CL #12), and BDO Seidman (CL #13)]. Although the means for achieving the clarification differ in some respects, they have in common the Board's objective of excluding joint ventures.
14. The Accounting Practices Committee of the United States Conference of Catholic Bishops (CL #3) suggested a revised merger definition that it believes would have the advantages of "excluding joint ventures and any other temporary arrangements, prevent[ing] dominance by any one party of the merger [and] substantially reduc[ing] the risk of an acquisition being incorrectly recorded as a merger." The Committee proposed the following definition:

A merger is the joining together of two or more previously independent not-for-profit entities by ceding the control each one formerly had to a single new (or reconstituted) not-for-profit entity, with none of the prior entities retaining either a withdrawal right or more than 50% representation on the new governing body, and with no donation or acquisition of net assets among the prior entities during or immediately preceding the process of joining together.

15. Similarly, in addition to the proposed condition that “the governing bodies of two or more not-for-profit organizations cede control of those organizations to create a new organization,” BDO Seidman (CL #13) proposed adding that the organizations that are parties to the transaction “are substantively absorbed into the new organization and cease to exist as separate organizations.” The respondent also explained that that absorption must be substantive, genuine, and not temporary to ensure that a merger is distinguished from an acquisition and a joint venture, in which two entities become three.
16. Charlotte Pryor (CL #16) proposed using a multi-conditioned definition that moves away from the notion of ceding control. Ms. Pryor suggested that a combination among not-for-profit organizations must meet the following requirements to be treated as a merger and accounted for using the carry-over basis:
  - a. No monetary consideration is paid or received or no consideration is exchanged beyond the assumption of liabilities; and either
    - (1) The purpose of the combination is to prevent loss of one or more of the combining organizations’ services to the community and to continue the organizations’ missions, which otherwise would not be possible due to the financial state of one or more of the combining organizations; or
    - (2) The purpose of the combination is to provide more services to the community than the total of the precombination organization; and
  - b. The mission and services of all precombination organizations must be retained by the resulting organization, with no loss in public service provision.

She suggested that this definition would better reflect that which distinguishes a not-for-profit organization from a for-profit entity. The public service concept embodied in her proposed definition relates to the reason not-for-profit organizations exist (to

provide a benefit to the public)—a reason “distinctly different from the *raison d’etre* of for-profit entities.”

17. PricewaterhouseCoopers (PwC, CL #15) suggested that the Board articulate a merger principle based on the following tenets:
  - a. The entities combine in their entirety.
  - b. Control is ceded to create a new organization.
  - c. No single entity acquires the other(s).

In addition, PwC suggested clarifying that in a merger neither organization acquires the other and supplementing the definition of a merger with a definition of an acquisition. Incorporating its suggestions, PwC proposed the following two definitions:

In a merger, the governing bodies of two or more not-for-profit organizations in their entirety cede control of those organizations to create a new organization; no one organization acquires the other(s). In an acquisition, one not-for-profit organization obtains control over the net assets of another organization or over an integrated set of assets and liabilities.

18. United Way of America (CL #7) suggested that the Board supplement the definition of control to include evidence of actual change in control. It and other respondents also suggested that the Board include examples of substantive evidence of a change in control indicative of a merger transaction. Some potential examples include contrasting:
  - a. A newly constituted board from a combining of existing boards
  - b. The creation of a new set of bylaws and articles of incorporation from adoption of those of one of the organizations
  - c. An absence of an opt-out clause from its presence
  - d. The existence of payments on or around the merger date from no consideration given beyond assumption of the others’ liabilities.
19. The Private Company Practice Session—Technical Issues Committee of the AICPA (CL #8) does not support a merger principle based on ceding of control. It stated that “the definition of a merger is not conceptually consistent with the principles established in Statement 141(R) and, as written, will not be operational in practice.”

Moreover, the Technical Issues Committee suggested that the definition of a merger be broadened to allow combinations with the following attributes to be accounted for using the carry-over basis of accounting:

- a. The merger involves contribution-based charities.
- b. No monetary consideration is paid or received or no consideration is exchanged beyond the assumption of liabilities.
- c. The purpose of the combination is to prevent loss of the acquiree's services to the community and to continue its mission, which otherwise would not be possible based on the acquiree's distressed financial state.

The Committee noted that the above criteria would include the occurrence of a "distressed merger" for which it suggested no goodwill should be recognized because goodwill implies that future economic benefits will be realized. However, during such a merger the "acquirer actually suffers economically from assuming the acquiree's liabilities."

### **Issue 3: Exclusion of Joint Ventures from the Scope of the Final Statement**

20. Question 3 of the Request asked respondents if together the definitions of merger and control make it sufficiently clear that transferring an integrated set of net assets to a newly created joint venture in which the transferor retains shared control does not equate to ceding control. Most respondents agreed that the two definitions, when taken together, make it clear that the aforementioned fact set does not constitute a merger, as control is not ceded but merely shared. Nevertheless, many of the respondents qualified their answers by conditioning their agreement upon revision of the definition of a merger, as discussed in Issue 1, to include additional criteria that would further narrow the definition in such a way that the exclusion of joint ventures would be more evident.
21. One respondent suggested that the Board make its intent clear by explicitly scoping out three forms of joint ventures: (a) "traditional" joint ventures, (b) the formation of a venture in which control is shared, but the sponsors do not share risks and rewards and retain no ongoing economic interest, and (c) similar transactions involving contributions of subsidiaries or integrated sets of net assets in which sponsors cede control by having equal representation on the initial board but thereafter the board is self-perpetuating [AICPA/AcSEC (CL #9)].

22. PwC (CL #15) suggested that the joint venture exclusion contained in the Exposure Draft be clarified by:
- a. Revising the language in paragraph 6(b) of the Exposure Draft to reflect the intent of the language in paragraph 2(a) of Statement 141(R), which reads as follows:

This Statement applies to a transaction or other event that meets the definition of a *business combination* in paragraph 3(e). This Statement does not apply to:

    - a. The formation of a joint venture.
    - b. Emphasizing that a merger involves the combination of two or more entities in their entirety by stating that fewer entities are created as the result of a merger while additional entities are created as the result of a joint venture
    - c. Broadening footnote 3 in the Exposure Draft to (1) acknowledge that venture-type transactions in the not-for-profit sector may have characteristics that differ from traditional ventures found in the for-profit sector, and (2) direct the reader to examples of transactions that are “in substance” joint ventures.
23. Girl Scouts of the USA (CL #14) suggested that shared control in the combined entity is not evidence that a ceding of control has not occurred and that, instead, the Board should look to other indicators such as whether a “new” organization is created and the fact that no one entity has control over the combined entity post-transaction. It also added that a percentage would be of benefit; it suggested that shared control be permissible as long as one of the entities does not have more than a certain percentage of the representation on the board.

#### **Issue 4: Additional Criteria and Guidance**

24. Question 4 of the Request asked respondents if the definition of a merger requires any additional criteria or guidance to address concerns about how to apply the guidance in instances of shared control and instances in which the combination contract contained an opt-out clause. Most respondents support the Board providing implementation guidance to aid preparers and auditors in applying the final Statement. Some respondents share the concerns of some Board members that without the additional guidance, preparers and auditors will be unable to properly distinguish between the different combinations and appropriately apply the Statement, especially with respect to joint ventures [Deloitte (CL #6) and Girl Scouts of the USA (CL #14)]. PwC (CL #15), however, stated that given the effort

and cost involved in structuring a combination as a merger, the ceding of control will be evident, especially if those suggestions outlined in paragraph 22 of this summary are incorporated into the final Statement. It added that independent auditors of the new organization are likely to participate in assessing the implications of the transaction as far as accounting is concerned, which should aid the auditor in determining whether a ceding of control has occurred.

25. Most of the implementation guidance desired by respondents revolves around the Board providing examples that demonstrate transactions that clearly qualify as a merger, acquisition, and joint venture as well as examples that clearly demonstrate transactions that do not qualify as a merger, acquisition, and joint venture. Half of the respondents also would like to see additional factors, examples, or both, that could be used to distinguish between the three types of transactions [Teresa Gordon (CL #2), Illinois CPA Society (CL #4), NYSSCPA (CL #5), Deloitte (CL #6), United Way of America (CL #7), AICPA/AcSEC (CL #9), Grant Thornton (CL #10), and Ernst & Young (CL #11)]. In addition, one respondent suggested that the Board include in the implementation guidance the results of the field visits conducted by the FASB [Illinois CPA Society (CL #4)].
26. Girl Scouts of the USA (CL #14) suggested that it may be prudent for the Board to require one or more of the following criteria to be met to qualify for merger accounting:
  - a. Common or similar missions
  - b. Common or similar customs
  - c. No monetary consideration exchanged
  - d. New bylaws
  - e. New policies and procedures.
27. Grant Thornton (CL #10) is against providing a detailed list of factors or rules to distinguish a merger from either an acquisition or the formation of a joint venture. Instead, it suggested that supplementary examples to aid in application of the guidance be provided in an appendix. Moreover, while some respondents would prefer additional guidance that provides examples, they raised concerns about how

doing so could move the Statement from being relatively principles-based to rules-based.

28. Furthermore, BDO Seidman (CL #13) suggested that the Board state that combination transactions are presumptively acquisitions. Additionally, it stated that unless the criteria in paragraphs 9–11 of the Exposure Draft cannot be applied to identify an acquirer **and** the definition of a merger (See Issue 1) is fulfilled in its entirety, a transaction should be treated as an acquisition.

### **Issue 5: Opt-Out Clauses**

29. Question 5 of the Request asked respondents if the presence of an opt-out clause would alone preclude the ceding of control from occurring. Most respondents agree that one or more parties' retention of an opt-out clause is sufficient evidence to determine that that party has not ceded control and, thus, would prevent the combination from being classified as a merger [Teresa Gordon (CL #2), NYSSCPA (CL #5), United Way of America (CL #7), AICPA/AcSEC (CL #9), Ernst & Young (CL #11), BDO Seidman (CL #13), and PwC (CL #15)]. PwC suggested that the inclusion of an opt-out clause would be a strong indicator that an acquisition occurred, as the primary purpose of an opt-out clause is to afford the acquiree some degree of protection.
30. Some respondents suggested additional guidance in a couple of areas:
  - a. Inclusion of additional criteria or guidance for determining the effect of opt-out clauses on the definitions of merger and acquisition and whether one (or the other) definition has been met [Illinois CPA Society (CL #4) and Deloitte (CL #6)]
  - b. Discussion of whether the existence of an opt-out clause affects whether or not a “consolidating event” has occurred in light of the recent revisions of guidance in FASB Staff Position SOP 94-3-1 and AAG HCO-1, *Omnibus Changes to Consolidation and Equity Method Guidance for Not-for-Profit Organizations* [AICPA/AcSEC (CL #9) and PwC (CL #15)]. If the existence of an opt-out clause does indeed affect the occurrence of a “consolidating event,” the final guidance should state so as practice is unlikely to recognize that both the recent revision to FSP SOP 94-3-1 and AAG HCO-1 and the opt-out clause provisions of the final Statement are linked [PwC (CL #15)].

31. Grant Thornton (CL #10) suggested that interpreting the proposed Statement in relation to the opt-out clause is not an appropriate task. Statement 141(R) is silent to the effect of an opt-out clause on the use of acquisition accounting in a business combination transaction and, thus, so too should be the final Statement on not-for-profit mergers and acquisitions.
32. One respondent suggested that an opt-out clause does not indicate that a merger has not taken place. Instead, the presence of an opt-out clause is merely evidence of good business practice and restricting its use to ensure a specific accounting method would not be prudent [Private Company Practice Session—Technical Issues Committee of the AICPA (CL #8)]. Other respondents merely stated that the facts and circumstances of each case and the terms of the contractual arrangement would have to be examined to determine whether or not the existence of an opt-out clause precluded merger accounting [Illinois CPA Society (CL #4), Deloitte (CL #6), and Florida Institute of CPAs (CL #12)].

### **Summary**

33. Overall, the comment letters demonstrated a general consensus that the underlying principle upon which the definition of a merger is based—the ceding of control—is appropriate. However, the letters suggested that the workability of the definition may be dependent upon (a) additional criteria, guidance, or both; (b) substantive revision or clarification of the merger definition; or (c) some combination of both (a) and (b). Many respondents also suggested that the Board clarify the scope of the Statement, especially as it relates to joint ventures. Lastly, most respondents agreed that the existence of an opt-out clause precludes the use of merger accounting.

**Exhibit A**  
**Comment Letter Index**  
**Request for Additional Comment**  
**Exposure Draft, *Not-for-Profit Organizations: Mergers and Acquisitions***

	<b>Respondent</b>	<b>Respondent Category</b>
1	Rosanna O'Guynn	Other—Individual
2	Teresa Gordon	Academic
3	United States Conference of Catholic Bishops (USCCB)—Accounting Practices Committee	NFP Preparer
4	Illinois CPA Society	Professional Organization
5	NYSSCPA	Professional Organization
6	Deloitte	Public Accounting
7	United Way of America	NFP Preparer
8	Private Company Practice Session—Technical Issues Committee of the AICPA	Professional Organization
9	AcSEC of the AICPA	Professional Organization
10	Grant Thornton	Public Accounting
11	Ernst & Young	Public Accounting
12	Florida Institute of CPAs	Professional Organization
13	BDO Seidman	Public Accounting
14	Girl Scouts of the USA	NFP Preparer
15	PricewaterhouseCoopers	Public Accounting
16	Charlotte Pryor	Other—Individual