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Letter of Comment No: 65
File Reference: 1204-001

October 28, 2005

Mr. Robert Herz
Chairman
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Project: Business Combinations
Reference Number: 1204-001

Dear Mr. Herz:

We would like to thank the Financial Accounting Standards Board (FASB) for the opportunity to comment on the impact of the FASB Exposure Draft, Proposed Statement of Financial Accounting Standards, "Business Combinations, a replacement of FASB Statement No. 141 ("the ED"). While our comments will primarily focus on our experience and views, we anticipate that many of the comments will be applicable to all registrants and will likely strike some commonality with others who choose to comment.

The ED was well intended and we support the FASB's effort to consistently apply accounting standards internationally. However, we do have some concerns with the current draft and do not support issuing the ED in its current form.

Below are our observations on the current ED:

Question 7: Do you agree that the costs that the acquirer incurs in connection with a business combination are not assets and should be excluded from the measurement of the consideration transferred for the acquiree? If not, why?

- As noted by the Board in paragraph B98, recognition of acquisition-related costs as an expense creates an inconsistency in accounting treatment under current GAAP as these costs are normally included in the carrying amount of an asset acquired outside the scope of a "business combination." In trying to eliminate perceived inconsistencies with regard to acquisition-related costs, another inconsistency is created. Internal and external comparability of financial statements could be impaired as assets acquired outside the scope of a business combination will have a higher cost base that negatively impacts earnings and return on investment as compared with assets acquired from a business combination, or similarly, fees incurred in obtaining financing or issuing debt. Similar to prior rationale relied upon in determining when costs should be capitalized, the company receives a future economic benefit from the

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acquisition on an ongoing basis. Therefore, these costs should be capitalized as required by current GAAP. The FASB should address the concern about inconsistencies by defining which costs can be capitalized. We believe the direct costs should be capitalized and indirect costs should be expensed as discussed in paragraph B94.

Question 8: Do you believe that these proposed changes to the accounting for business combinations are appropriate? If not, which changes to the accounting for business combinations are inappropriate, why and what alternatives do you propose?

- While we support the FASB's goal toward measuring acquired assets and liabilities at fair value, we do have some concerns with the proposed changes particularly as they concern contingencies. The proposed change seems to create another inconsistency for accounting for contingencies assumed in an acquisition versus those outside of the scope of a business combination. As an example, a potential contingent customer claim liability for an existing operation may not require accrual under FASB Statement No. 5, Accounting for Contingencies, while the same type of potential liability assumed in a business combination would be required to be recorded at its fair value. Even if recorded under Statement 5, the amount accrued under Statement 5 could differ from the amount determined under a fair value concept. Further, subsequent changes in the accrual could also be inconsistent. We recommend contingencies be determined under Statement 5.
- While we do not fully disagree with the proposed change for measuring acquired receivables, our observation is that this could, along with proposed changes concerning the measurement date, result in an unintended impact on earnings. Under current practice, a valuation allowance for the uncollectible accounts receivable is usually established based on information at the acquisition date. As most accounts receivables would generally be collected within the one-year measurement period, at the end of the measurement period the valuation allowance is adjusted for those receivables collected for which an allowance was originally established. The adjustment of the valuation allowance would only impact goodwill, not be reflected as an immediate gain. With the proposed change, collection of the receivable would result in an immediate gain in the income statement. We recommend the FASB formalize the current practice.
- We are also concerned with the proposed change that requires restructuring or exit costs to be treated as a post-combination expense. We do not believe this treatment adequately reflects the fair value of the acquisition. Often acquisitions are only consummated based upon synergy plays. The closure of acquired plants or operations are often contemplated in the synergy plays and in consummating the transaction. They are often at least indirectly contemplated in the transaction price. Therefore, the impact of planned restructuring and exit activities must be considered in the valuation of the acquired assets and liabilities. We believe the concepts of EITF 95-3 should be incorporated in the revision of Statement 141. We also continue to agree with current accounting practice that any restructuring activities that impact operations, employees or plants that are not acquired in the business combination should be reflected as expenses in the post-combination period.

Question 9: Do you believe that these exceptions to fair value measurement principle are appropriate? Are there any exceptions you would eliminate or add? If so, which ones and why?

- Regarding the proposed change concerning deferred tax benefits that become recognizable because of the business combination are not part of the fair value of the acquiree, and should be accounted for separately from the business combination, we prefer not to comment on the proposed change until the FASB resolves accounting for uncertain tax positions. We do recommend that any final determination be based on consistent application with any final determination on uncertain tax positions and other existing pronouncements.

Question 13: Do you agree that comparative information for prior periods presented in financial statements should be adjusted for the effects of measurement period adjustments? If not, what alternative do you propose and why?

- The proposal requires a restatement of previously issued financial statements for adjustments made to the initial provisional estimates of values during the measurement period. We do not agree with this proposed change to measurement period adjustments. The current practice takes into consideration the effort required and judgments made in making initial provisional estimates. The valuation process, including obtaining third party appraisals, can often take many months and often does not even commence until after the acquisition date. Consequently, there are often changes in the provisional estimates during the measurement period. The changes in the valuations of the assets and liabilities should be reflected in the period the estimate changes and reflected as an adjustment to goodwill with the exception of those changes that impact asset or liability bases that would have impacted the base for depreciation or amortization or have other income effect. The market usually negatively views financial statement restatements. A very unintended market result could occur if a restatement occurs for adjustments that even the FASB would readily admit are anticipated and based on estimates that are very difficult to estimate at the initial acquisition date. We therefore recommend that adjustments that impact depreciation, amortization and other income items be made in the period the estimate is changed. This is consistent with existing guidance. We concur with the time of the measurement period.

We appreciate the opportunity to express our views and would be pleased to discuss our comments or answer any questions you may have. Please do not hesitate to contact us regarding this letter.

Very sincerely yours,

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