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Regarding: Business Combinations -805- Supplemental Pro-forma Data Technical Director: EITF - 100G

Comments By: Dr. Joseph S. Maresca CPA, CISA

Colleagues,

Thank you for the opportunity to critique this issuance.

Details follow.

Background

805-10-50-2h requires a public entity to disclose pro-forma information for business combinations in the current reporting period and the acquisition date for business combinations occurring that year as of the beginning of the annual reporting period. pp. 1

The intent is to clarify the acquisition date for pro-forma information when the comparative financial statements are presented. pp. 2 **I concur.**

Ouestions Presented for Comment:

- (1) Should the acquisition date be as of at the beginning of the prior annual reporting period unless something significant occurs?
- (2) Should there be additional disclosures of the nature of non-recurring pro-forma adjustments which provide useful data. c/f SEC- 8K Article 11 of Regulation SX.
- (3) Should amendments be proposed prospectively?
- (4) Is the effective date too soon to afford meaningful and timely compliance by the preparers of financial statements?

For each combination, disclose the following:

- (a) description of the acquiree
- (b) acquisition date
- (c) the percentage of equity ownership interest acquired
- (d) the reason for the acquisition and how acquirer gained control of the

acquiree pp.3 I concur.

For business combinations happening in stages, disclose:

- (a) the acquisition date fair value of the equity interest
- (b) the gain or loss recognized with respect to remeasuring to fair value the equity interest in the acquiree held by the acquirer immediately preceeding the business combination
- (c) the valuation techniques used to evaluate the acquisition date fair value of the equity interest in the acquiree held by the acquirer immediately before the business combination

These valuation techniques could be complicated by the factors noted below under "Acquisition date values may be complicated by the following". (see below)

GHG or Greenhouse Gas Compliance could be another difficult

valuation issue, as argued below.

(d) information enabling the users of financial statements to assess inputs used to develop the fair value measurement of the equity interest of the acquiree held by the acquirer immediately before the business combination

If the acquiree is a public business entity disclose:

- (a) revenue and earnings of the acquiree since the acquisition date included in the consolidated statements of the reporting period
- (b) if comparable statements aren't presented- revenue and earnings of the combined entity for the current report period as though the acquisition for all business combinations that occurred during the year had been as of the annual period (supplemental pro-forma information)
- (c) if comparative financial statements are presented, the revenue and earnings of the combined entity as though the business combination occurring in the current year had occurred at the beginning of the comparable prior annual reporting period
- (d) the nature and amount of any material non-recurring adjustments directly attributable to the business combinations included in pro-forma revenue and earnings . pp. 6 (supplemental pro-forma information)

Critique

Under ASC 805, accounting for business combinations applies to a broader range of transactions and triggering events including acquisitions of some enterprises in the developmental stage, combinations of mutual entities, acquisitions without the exchange of consideration, and the initial consolidation of a variable interest entity that is in substance a business. ASC 805 constructively eliminates the cost-based purchase method under Statement 141.

In general, ASC 805 requires acquisition-date fair value measurement of identifiable assets acquired, liabilities assumed, and noncontrolling interests in the acquiree. Under ASC 805, the value of the business acquired is measured generally as the sum of the acquisition-date values .

Acquisition date values may be complicated by the following:

- o major derivative contracts and counterparty interests on the part of the acquiree
- o major intercompany transactions that are not "at arms length"
- o out-of-date equipment and facilities which have been fully depreciated earlier or material non-compliance with the EPA Greenhouse Gas Guidance may necessitate significant investments or customizations to achieve compliance milestones
- o major stock market or host country instability affecting valuations of the acquiree or its investment portfolio
- o preferred stock of the acquired company or acquiree
- o practical consolidation of the data processing systems of the acquiree and the consolidated entity
- o the need for "Cloud Computing" to facilitate data protocol standardization

Risks in derivative transactions are a function of the following items: (including these types of transactions in consolidation)- (Source: OCC 4th Quarter Report '03)

o counterparty exchange of nominal principal

- o volatility of interest rates and currencies used to determine the contract payments
- o the maturity and liquidity of contracts
- o creditworthiness of counterparties in the transaction

The degree of risk is a function of:

- o aggregate trading positions
- o asset and liability structures of the consolidating entities
- o data describing fair values and credit risk exposure is more useful for point in time risk exposure
- o data on trading revenues and contractual maturities for consolidating entities

These complicating factors could impact the acquisition date unpredictably. This is the subject of Question 1. Additional disclosures pertinent to SEC Reporting of non-recurring events could have significance to Question 2- Additional Disclosures. The effective date may be too soon to satisfy the timeliness inherent in Question 4 provided for member comment.

Specifically, ASC 805 also may impact deferred taxes that cause deferred tax assets and deferred tax liabilities, as well as the potential need to record a valuation allowance for them. A valuation allowance for these is created based upon the potential that the asset or liability will not be realized in the future.

When a company incurs certain types of losses, it may be allowed to carry these forward and apply them against future income. A situation may occur; wherein, a company doesn't have enough income to apply tax credits recorded as deferred tax assets being carried forward from a previous year or prior years. c/f. pp. 1 implications

The underlying rationale of Statement 109 is that deferred tax assets and liabilities should be recognized for the future tax consequences of past events. Both are measured and recorded based upon the expected tax consequences when the underlying temporary differences (book- versus tax-basis differences) generate future taxable income or deductions. In addition to temporary differences, deferred tax assets also are recognized for tax attributes such as operating and capital losses, as well as tax credit carryforwards.

Greenhouse Gas EPA Compliance may be another issue in consolidating the entities, as well as reporting additional disclosures in anticipation of EPA compliance for equipment and facilities of consolidated entities. The most important question involves whether or not the consolidated entity can comply with the EPA Guidance without major expenditures on plant and equipment to modernize the plant operations in accordance with the requirements set forth below. *The items below may be pertinent to the determination of Questions 2 and 4 in the above.*

The Environmental Protection Agency (EPA) in the USA has set forth statistical data on emissions. CO2 is responsible for approximately 85% of all emissions.

The relevant statistics are:

Source: http://epa.gov./climate change/emissions/co2/human/htm www.epa.gov

Extrapolating from this estimate of the EPA, most industrial entities should

fall within the following band:

Fossil Fuel Consumption
Non-energy use of fuels
Natural Gas Systems
Muni Solid Waste
Annonia Production and Urea Consumption
Other

160 units
140 units
26 units
25 units
13 units
5 units

Totals 369 units

369/519 = 71% of all emissions

The remainder of the emissions deal substantially with manufactures. i.e. Iron and Steel Production, Cement Manufacture, Lime Manufacture, Limestone/Dolamite Use, Aluminum Production and Petrochemical Production. Cropland may be disaggregaged, as well.

Practically speaking, these estimates provide a quantifiable benchmark for GHG emission discussions on the financial statements . Where each member state of IFAC has an Environmental Protection Agency or its equivalent, workable benchmarks may exist already for use by industry in quantifying GHG in practical terms.

Organizationally, the Purchasing Department is the source for minimizing CO2 emissions during the conduct of routine purchasing decisions. Corporate purchasing standards should require purchasing products, systems and processes to have a minimum CO2 footprint or impact on the entity. The government can help this process by providing generous tax credits for the purchase of GHG equipment with a marginal environmental footprint.

For instance, the purchase and installation of an Advanced Scrubber should provide a quantifiable deduction of emissions in the guarantee statement by the manufacturer. In addition, advanced scrubbers are protected by patent filings which teach the scientific art resulting in the award of the patent. At least in the USA, the Patent Office (PTO) has mechanical and chemical examination divisions which examine the new use and uniqueness of the claimed inventions- particularly those dealing with advanced scrubber technology. i.e.

New materials are on the horizon; such as, cell based bioplastics, starch bioplastics, plastarch, polylactic acid and polyamide. Thermoelectrical and piezo electric systems are slated to replace batteries. Engineering certifications which accompany the purchase of these products are a source of a deduction of standard emissions in the aforementioned technologies and processes.

US-PTO Patent # 5354364 provides improved efficiency for an advanced dry scrubber. Issued 10 -11- 1994

The present invention resides in a high efficiency advanced dry scrubber (HEADS). The purpose of the invention is to advance the existing dry scrubbing technology by increasing both sulfur oxide/contaminant removal efficiencies and reagent utilization to approach those achievable by wet scrubbing, by reducing spray down temperatures to at/or near saturation while still producing a dry product.

In addition, the Department of Engineering, Maintenance Engineering or Building Engineering routinely monitor plant environmental controls and maintenance through internal record-keeping and ongoing environmental monitoring of systems and processes. These areas of the consolidated organization would provide a good potential source for obtaining the requisite assurance internal to the organization in coordination with the corporate legal counsel, the public accounting firm and the financial and IT internal auditors.

Goals of the GHG Guidance:

The guidance seeks to accomplish the following:

- (1) Quantification of GHG emissions, regulatory disclosure and emissions trading
- (2) Establishment of an Engagement Partner, team of accountants/auditors and experts
- (3) Providing better reporting data on the susceptibility of GHG statements to error
- (4) Development of GHG competencies in assurance, GHG scientific principles, industry experience and the advice of experts

Critique:

(1) How do experts operate?

The expertise in GHG will be implemented by the Engagement Team consisting of the Partner, accountants/auditors, relevant legal counsel, management experts, expert witnesses (where appropriate), the entity department of engineering for manufacturers and data from the Environmental Protection Agency or its equivalent in foreign countries, states or municipalities.

Technologically, the patent office is the originator of new art in advanced scrubber technology and advances in chemical composition methodologies, processes and machinery. The area of artificial intelligence has advanced state-of-art "Advice Giving Systems" which aggregate the advice of experts onto a centralized database by the knowledge engineer. Programming languages; such as, Prolog, Lisp and SAIL are utilized to implement artificial intelligence systems in practice. External experts should be independent to avoid manipulation of the process or the appearance of manipulation of the process. Transparency is another important concern which can be helped by independence for GHG.

- (2) The working draft is not complete in so far as foreign legal venues. Contract legalese, choice of language, differences in GHG practices and choice of legal venue to enforce contracts are all limiting factors which impede uniformity. Existing treaties help reduce these limitations; however, treaties are subject to compliance verification and positive *moral suasion* by the host governments.
- (3) Are assertions accurate with respect to identifying the risks of a material mis-statement?

The accuracy of assertions will be subject to the experiential domain over time, as well as industrial experience. Local governmental compliance examinations will provide better information which will impact assurance more convincingly. i.e. Examinations of the Environmental Protection Agency , state, province and local governments (including their foreign equivalent bureacracies)

(4) Can practitioners provide risk assessment at the assertion level for GHG engagements or major consolidations involving GHG issues? Why or why not?

Over the passage of time, practitioners should be able to make these assertions based upon:

- (a) guarantees by manufacturers on new purchases of pollution control equipment
- (b) the examinations of the Environmental Protection Agency and local governments and the use of artificial intelligence and "Advice Giving" systems
- (c) the analysis of experts in the engineering and chemical art
- (d) manufacturer departments of engineering, maintenance engineering and environmental engineering
- (e) the input of patent attorneys at the point of creation of scientific patents
- (5) What are the most significant risks of GHG at the GHG statement level?
- (a) uncontrollable risks like adverse weather, volcanic eruption, tsunamis and earthquakes
- (b) MTBF or variation of the expected mean time between failures of pollution control equipment
- (d) contingencies and disaster recovery, power outages etc.

These risks may be mitigated by disaster recovery and contingency planning in the consolidated entity.

(6) Assurance that the subject matter is free from material error

The review of prior year workpapers, discussions with management/legal counsel, management experts and independent external experts help mitigate these risks. GHG examinations by local governments also help to mitigate these risks. A national Environmental Protection Agency or its equivalent or governmental unit may help to aggregate the data into a national profile with constituent subunits or parts.

(7)
How can GHG be aggregated and related to the income statement or balance sheet?

The aggregation of GHG is a national effort with local standards implemented by cities, municipalities and individual counties. GHG can be related to the P & L by municipal fines, tax credits and cost reductions due to new technologies and patents.

(8) Special purpose criteria may be implemented during the testing phases of new products and processes in the department of engineering.

Emissions deductions may be made from various activities; such as, planting trees, purchasing of advanced scrubbers, major concensus from artificial intelligence systems reporting communities of expert advice, the GHG examinations of national and local government auditors and environmental test data.

Indirect emissions can be taxed locally.

Limited assurance may be distinguished from reasonable assurance depending upon the extensiveness of the GHG statement or a limited purpose set forth at the outset of a special audit. For instance, an auto manufacturer seeks to test a new catalytic converter at an early stage of production. A limited assurance engagement could report on the findings of management's internal and external expert for monitoring by the Board of Directors. These types of issues will complicate entities in the process of consolidation.

Reasonable assurance may be expressed in the audit of a data center for compliance with EDP or IT standards and environmental controls relating to heat, power and light systems and the disposal of waste products. Disaster recovery, UPS (uninterruptible power source) and contingency planning assists in providing reasonable assurance. *These IT issues are pertinent to entities considering consolidation*.

A reasonable assurance engagement has predictability and previous audit experience, work papers etc. A limited assurance engagement is in the nature of specific purpose, new process, new equipment or expert statement provided for a court review.

- (9) The *sink* is the physical process which removes GHG from the atmosphere. Such a process is a patent; such as, an advanced scrubber or the purchase of pollution control equipment/processes which enhance removal of the GHG.
- (10) Risks of material mis-statement are mitigated by:
- o understanding the entity
- o inquiries within the entity
- o analytic procedures and standards
- o observation and inspection

The engagement team will perform analytics; such as, flow charts and systems analysis to document the system of internal control as applied to GHG. The Purchasing Department, Department of Engineering, Legal Counsel, Financial and IT Internal Auditors, reports of the Environmental Protection Agency (or its foreign equivalent), scientific journals and patent art are all good sources for performing analytics. Prior year workpapers are additional sources. External experts who are independent may be engaged to assist in this process. The Data Processing Department is another source because environmental controls apply to the ongoing operation of data center operations for the consolidated entity and its related entities in whole or part.