October 28, 2005

Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856

Re: Proposed SFAS – File Reference 1204-001

Dear Director:

On behalf of QUALCOMM Incorporated, we respectfully submit this comment letter on the Proposed Statement of Financial Accounting Standards, Exposure Draft on Business Combinations. We have limited our response to selected questions posed in your Exposure Draft.

Question 3—In a business combination in which the acquirer holds less than 100 percent of the equity interests of the acquiree at the acquisition date, is it appropriate to recognize 100 percent of the acquisition-date fair value of the acquiree, including 100 percent of the values of identifiable assets acquired, liabilities assumed, and goodwill, which would include the goodwill attributable to the noncontrolling interest? If not, what alternative do you propose and why?

In situations where there is a pre-existing, noncontrolling interest and then the acquirer obtains control, we do not agree that it is appropriate to recognize 100% of the acquisition date fair value of such acquiree. Recognition of 100% of the acquisition date fair value could result in a significant increase in the recorded values of the noncontrolling interests. Although this proposed accounting treatment would eliminate the current practice of reporting book values that are comprised of a combination of historical book value for the noncontrolling interest’s proportional interest and fair value for the controlling interest’s proportional interest, an increase in the recorded values of the noncontrolling interests would increase recorded goodwill. The potential for higher recorded values of goodwill which could result seems problematic for several reasons:
a. Additional goodwill is created without commensurate new investment in the acquired entity. Higher goodwill balances increase the likelihood of subsequent impairment charges; as such, income statement volatility could increase as a result of a write up of assets that did not result from a substantive economic event;

b. The fair value of noncontrolling interests may be difficult to determine since the amount paid for a controlling interest typically includes a control premium;

c. Purchase transactions in which the acquirer of the controlling interest was previously a minority shareholder may result in a gain to the acquirer. This result would be contrary to guidance on accounting for transactions between related parties (as discussed in further detail in the response to Question 10).

Question 4—Do paragraphs A8-A26 provide sufficient guidance for measuring the fair value of an acquiree? If not, what additional guidance is needed?

There are significant challenges in measuring the fair value of an acquiree which will include a high degree of uncertainty. Valuation techniques used will likely contain a significant amount of inputs that are not readily obtainable from observable markets, increasing the subjectivity involved. Therefore, we believe that significantly more guidance on estimating fair values should be provided. Additionally, we believe that the conclusions in this Exposure Draft should be consistent with those provided in other FASB projects (e.g. the Conceptual Framework Project, the Financial Performance Reporting Project, the Fair Value Measurements Project, and the Liabilities and Equity Project) when completed.

Question 5—Is the acquisition-date fair value of the consideration transferred in exchange for the acquirer’s interest in the acquiree the best evidence of the fair value of that interest? If not, which forms of consideration should be measured on a date other than the acquisition date, when should they be measured, and why?

We agree that the fair value of the consideration transferred in exchange for the acquirer’s interest in the acquiree is the best evidence of the fair value of that interest. However, we believe acquisition consideration should be measured on the earliest date on which the terms of the acquisition are agreed to and announced or the date of final application of the formula pursuant to the acquisition agreement that determines the number of the acquirer’s shares or other consideration to be issued, consistent with current practice under EITF 99-12, “Determination of the Measurement Date for the Market Price of Acquirer Securities Issued in a Purchase Business Combination.” If both parties have made commitments and established the terms of the arrangement, conditions that change after both occur are usually outside the control of the acquirer and are not indicative of the exchange agreed to between the parties.
Furthermore, the acquirer's stock may be highly volatile. When stock is issued by the acquirer to effect an acquisition, the use of the acquisition date to value equity interests issued by the acquirer could result in inflated goodwill values if the stock price increases between the date the terms are agreed upon and the acquisition date. Impairment charges could result that otherwise would have been avoided and that do not result from the acquired entity's performance failing to meet the acquirer's expectations. Conversely, stock price declines between the measurement date and the acquisition date would result in recording the acquisition at a value less than what the parties agreed to based on the arm's length negotiations concluded at the measurement date.

Question 6—Is the accounting for contingent consideration after the acquisition date appropriate? If not, what alternative do you propose and why?

We do not believe that the accounting for contingent consideration at and after the acquisition date is appropriate. Contingent consideration may relate to resolution of asset valuation or liability resolution associated with the pricing of a transaction. Earn-out targets may be utilized when there is a disparity between the buyer's and the seller's estimates of the earning power of the business. If contingent payments are made in excess of the estimated fair value of a liability because the acquiree has outperformed expectations, recording losses in the subsequent periods would seem inappropriate and misleading. In other cases, contingent consideration arrangements may merely represent deferred payout, and as such, should not logically result in post-acquisition gains or losses.

Measurement of contingencies and contingent consideration at fair value also carries an unacceptably high risk of error and manipulation. An acquirer will have an incentive to be overly conservative in establishing liabilities at their maximum possible value in order to mitigate remeasurement losses in subsequent periods. This approach will increase the likelihood of significant remeasurement gains in subsequent periods if the final outcome is lower or does not occur at all. We agree with the alternative view expressed in paragraphs B206 through B208 that such fair value measures will be "artificial constructs that lack representational faithfulness with actual economic phenomena."

We also question the relevance and reliability of such fair value measures and the subsequent accounting gains and losses that would result from their use. Many contingencies are outside the control of the acquirer. As a result, remeasurement gains and losses reported in net income related to an acquirer's contingent consideration arrangements would not relate to the acquirer's ongoing operations. We question the relevance of such gains and losses to users of financial statements; in particular, such information will not enhance a user's ability to predict future cash flows of the acquirer. Furthermore, these new types of gains and losses would add to the challenges of effective communication in financial statements.
We believe that contingent consideration should be valued at the date the contingency is resolved and continue to be recorded under FAS 141, "Business Combinations," in which any contingent consideration payable by the acquirer is recorded as additional purchase consideration and goodwill as such amounts become determinable.

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?

No, we do not agree. We believe that acquisition-related costs, such as accounting, legal and valuation consultant fees, are essential requirements of business acquisitions and are common to any acquirer. As such, we believe that these costs are part of the total purchase price paid by the acquirer. This concept is consistent with the application of generally accepted accounting principles in other areas whereby acquisition-related costs are treated as part of the carrying amount of the related asset. For example, transaction costs are capitalized as part of the cost of acquiring marketable securities and various third party costs, such as site assessment fees, are capitalized as part of the cost of property, plant and equipment. We do not believe that the method of acquisition should result in a different accounting treatment for acquisition-related costs. We also find the inconsistency in accounting treatment (i.e. capitalize vs. expense) troubling and not helpful to preparers. Expensing of acquisition-related costs separately from the purchase consideration may also distort the presentation of an acquirer’s earnings and cash flows, adding to the complexity for investors and other users of financial statements.

Furthermore, the total cost of the acquisition (i.e., the consideration plus all out-of-pocket expenses) is considered in the investment decision. The fair value of a target company to any acquirer must equal or exceed the total cost of the investment, including acquisition-related costs, to support an investment decision. The acquirer uses the total purchase price to forecast the transaction’s internal rate of return (IRR), impact on earnings, and other performance metrics.

Finally, we believe there is potential for inconsistent treatment between the seller’s and acquirer’s transaction costs. Since the seller’s costs are generally assumed liabilities (or if paid, reduce acquired cash balances) that reduce the net assets of the acquiree, the Exposure Draft would permit the seller’s costs to continue to be capitalized as additional goodwill. Conversely, costs paid by the acquirer would be expensed. Disparate treatment of acquisition costs could impact the structure and terms of acquisitions.

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

a. Receivables are primarily comprised of amounts due from customers for products and/or services rendered and are typically maintained in a detailed subledger. The
use of a valuation allowance allows the acquirer to maintain the details of historical transactions for future collection and tracking efforts, while achieving the goal of recognizing the fair value of the receivable assets as of the acquisition date. For these practical purposes, we believe that recognition of a separate valuation allowance is appropriate.

b. We believe that the acquisition of a contingent asset or liability does not change the contingent nature of such asset or liability, and therefore the recognition of a contingent asset or liability should be consistent with the accounting for contingencies acquired or incurred in an event other than a business combination in accordance with FAS 5, "Accounting for Contingencies." Furthermore, valuation of these assets and liabilities will be administratively burdensome and subject to variability among companies.

c. We believe that costs associated with restructuring or exit activities are liabilities as of the acquisition date if these activities were contemplated by the buyer at the time of acquisition. Such costs should be considered part of the total purchase price paid by the acquirer as they are usually necessary to achieve the contemplated synergies and business projections resulting directly from completing the combination. These synergies and related costs are significant determinants in the acquirer's decision to effect the purchase and related restructuring and are used to forecast the transaction's impact on earnings, IRR and other business performance metrics. Such costs would typically be borne by any acquirer and are not relevant to the acquirer's post-acquisition operating results.

If such restructuring plans are identified at the time of acquisition (as opposed to a later operating decision) and the acquirer's management committed to a plan to restructure, we believe provisions should be established for such costs and included as part of the purchase price, regardless of their meeting the criteria in FAS 146. As such, costs incurred for restructuring or exit activities related to an acquired company should continue to be recognized as liabilities at the acquisition date consistent with current practice under EITF 95-3, "Recognition of Liabilities in Connection with a Purchase Business Combination.”

d. We believe that the acquisition of in-process research and development does not change the nature of those ongoing efforts, and therefore, the recognition of in-process research and development ("IPR&D") should be consistent with the accounting for research and development efforts in the normal course of business under FAS 2, "Accounting for Research and Development Costs." This is also consistent with the expensing of IPR&D that is required in an asset acquisition. We do not believe that the method of acquisition should result in a different accounting treatment for IPR&D.
Question 9—Do you believe that these exceptions to the fair value measurement principle are appropriate? Are there any exceptions you would eliminate or add? If so, which ones and why?

Yes, we believe these exceptions are appropriate. Furthermore, we believe reference to guidance provided by other GAAP that addresses specific concepts should be consistent throughout the guidance with respect to business combinations as noted elsewhere in this letter.

Question 10—Is it appropriate for the acquirer to recognize in income any gain or loss on previously acquired noncontrolling equity investments on the date it obtains control of the acquiree? If not, what alternative do you propose and why?

We believe that it is not appropriate to recognize in income any gain or loss on previously acquired noncontrolling equity investments on the date the acquirer obtains control of the acquiree based on the concept that no transfer or exchange has occurred with respect to the noncontrolling equity investment (i.e. the acquirer retains its current interest and adds to it for a combined investment). As such, no economic gain or loss has been realized. The fair value of the consideration transferred should be recorded as an additional investment in the acquiree.

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?

We do not agree that comparative information for prior periods should be adjusted for the effects of measurement period adjustments. Notwithstanding the practical difficulties and the cost/burden on preparers of assembling this information on a timely basis, retrospective adjustments to previously issued comparative information may undermine the reliability and credibility of financial reporting. Since adjustments to any provisional amounts that were recognized at the acquisition date represent changes in estimates that result from new information, they should continue to be accounted for in (a) the period of change if the change affects that period only, or (b) the period of change and future periods if the change affects both in accordance with current treatment under APB 20 “Accounting Changes” and for future periods under FAS 154, “Accounting for Changes and Error Corrections.”

Question 15—Do you agree with the disclosure objectives and the minimum disclosure requirements? If not, how would you propose amending the objectives or what disclosure requirements would you propose adding or deleting, and why?

We agree with the disclosure objectives and minimum disclosure requirements with the exception of the requirements in paragraphs 72(d), 72(e) and 74(a). Therefore, we recommend that these requirements be deleted.
We believe that disclosure of a description of the factors that contributed to goodwill as required by paragraph 72(d) would be difficult as such factors may not be clear other than the cost of the business exceeded the fair value of the identifiable net assets acquired.

We believe the disclosure of the acquisition-date fair value of the acquiree and the basis for measuring that fair value as required by paragraph 72(e) would be confusing and misleading. The enterprise fair value of an acquiree based on a market participant approach often differs from the purchase price for reasons that are difficult to quantify and explain. For example, synergistic value of the acquiree to the acquirer is a significant factor in determining the amount and type of consideration the acquirer is willing to transfer which is further influenced by negotiations between the parties. Furthermore, the proposed standard states that, in the absence of evidence to the contrary, the best evidence of the fair value of the acquirer’s interest in the acquiree is presumed to be the fair value of the consideration transferred, rendering the disclosure requirement inconsistent and irrelevant.

We also strongly disagree with the requirement in paragraph 74(a) with respect to the disclosure of the amounts of revenue and net income of the acquiree after the acquisition date in the consolidated income statement for the reporting period. Operations of the acquiree are often integrated with those of the acquirer and are not managed separately in which case there is often no separate internal reporting of revenue and net income for the acquired company. If discrete financial information is available for the acquired company after the acquisition date, this information can be meaningless and misleading. Discrete information may represent only a portion of the acquired entity post-acquisition due to integration. Alternatively, the acquired entity’s standalone operations may have been an immaterial component of the value of the acquisition to the acquirer which drove the purchase price. As such, the discrete information about the acquired entity would be confusing and misleading to users of financial statements.

Thank you for the opportunity to comment on the Exposure Draft.

Sincerely,

William E. Keitel
Executive Vice President and Chief Financial Officer
QUALCOMM Incorporated