October 12, 2005

Ms. Suzanne Q. Bielstein
Director of Major Projects and Technical Activities
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5112
Norwalk, CT 06856-5116


Dear Ms. Bielstein:

Please accept the enclosed comments on the Board’s proposed replacement of FASB Statement No. 141. The comments represent perspectives of students currently enrolled in the Indiana University Kelley School of Business Indianapolis MPA Program. We appreciate the opportunity to respond to the Exposure Draft and hope that the Board will take our suggestions into its consideration.

After reviewing and discussing the proposed draft, we are pleased to provide the following comments specific to certain key questions raised by the Board in the 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 alternatives do you propose and why?

We agree with the Board that it is appropriate to recognize 100 percent of the acquiree’s assets acquired, liabilities assumed, and goodwill when a business holds less than 100 percent of the equity interest in the acquiree. The Board stresses the presence of acquirer’s control in the business combination. Paragraph 6 describes possible ways an acquirer might obtain control over an acquiree: (a) by obtaining the equity interests, (b) by acquiring some or all of an entity’s assets, and (c) by assuming some or all of the liabilities of an acquiree. In all of these situations, the acquirer has the ability to influence net assets after the acquisition. Therefore, we find that combined financial statements of the acquirer after the acquisition should reflect the economic reality of the transaction by recognizing 100 percent of net assets and goodwill and simultaneously recognizing the non-controlling shareholders’ interest in the net assets as a separate component of stockholders’ equity.

We support the Board’s proposal to recognize goodwill at its full fair value. In our opinion the new method is a more reasonable measurement of goodwill and is more consistent with objectives set by the Board. Under current GAAP, goodwill in a business combination is measured as the difference between acquirer’s consideration paid (plus costs associated with the acquisition) and fair value of the net assets.
associated with ownership percentage purchased. This results in recording only the parent entity's share of goodwill and omitting portion related to noncontrolling interest. This practice contradicts the fundamental principles underlying this Statement. We believe that once the Board made a decision in Statement No. 141 to make the acquisition method the only method of accounting for business combinations, the method is to be applied consistently. According to paragraph B23(c) of the Exposure Draft, "the total amount to be recognized for the acquiree should be the fair value of the acquiree as a whole." This underlying principle will be incomplete without recognizing that goodwill is to be measured at full fair value as part of the acquiree's assets (and noncontrolling equity). We see it as a significant improvement to reporting of business combinations.

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?

This Exposure Draft proposes that acquisition-related costs that the acquirer incurs which are related to a business combination should be excluded from the measurement of the consideration transferred for the acquiree because those costs are not part of the fair value of the acquiree and are not assets. We strongly disagree with the Board in this matter. In our opinion, the actual costs of the acquired entity and acquisition-related costs should both be recorded as part of the transaction – the two should not be separated. Acquisition costs, such as accounting, valuation, and legal fees, among others, are essential costs that an entity must incur if it wishes to acquire another entity. These unavoidable transaction costs should be capitalized as a portion of the total investment in the business.

Assigning costs to the purchase of a business should be treated the same as assigning costs to the purchase of an individual asset. For example, GAAP allows for transportation and setup costs to be included in the carrying value of a fixed asset. These components may not increase the fair value of the asset, but they are essential in getting the asset into a productive state. We feel that acquisition-related costs should be treated in the same manner. While these particular costs do not directly increase the fair value of the business being acquired, they are absolutely necessary in completing the business combination. If acquisition-related costs are expensed in the period incurred, earnings for the period will be understated. Because the purchase of a business entity leads to "probable future economic benefits" over an extended time, acquisition costs related to the purchase should be expensed over an extended period of time and not all at once.
Question 8 – Do you believe that these proposed changes (measuring and recognizing assets and liabilities acquired) to the accounting for business combinations are appropriate? If not, which changes do you believe are inappropriate, why, and what alternatives do you propose?

We comment on three changes.

Part (b) relates to an amendment of FASB Statement No. 5. We agree with this proposed change. There is a debate in the prior comment letters about this issue. Some responders believe that recording non-financial liabilities at fair value makes little sense because it will produce financial statement results that are neither relevant nor reliable. Some responders believe the uncertainty inherent in such contingency valuations will be eliminated with clear assumptions and unbiased basis for the assumptions. Our opinion is that the contingencies should be and can be recognized within a reasonable range of possible outcomes. It is rational for the enterprise management to determine sound range of outcomes with available information and to produce a reasonable estimate of contingent liabilities. (1)

Part (c) pertains to costs associated with restructuring activities. We disagree with this proposed change. Even though costs the acquirer expects to incur in the future pursuant to its plan to exit arc not present obligations, the acquirer has taken these costs into consideration when setting the purchase price. "And the acquirer is probably irrevocably committed to the exit plan on the communication date because, at that time, employees can be expected to look for new jobs and may not be available if the entity revises its plan." Therefore, we believe if management has committed to a plan to restructure, the exit costs should be recognized as a liability.

Part (d) deals with research and development costs. We agree with the Board that the research and development assets acquired in a business combination that previously were required to be written off would be recognized and measured at fair value. "The value of the right to enhance or embellish an existing product (In-Process R&D), or an existing technology that has alternative future uses, is not separable from the value of the intellectual rights to the technology." If the R&D assets are recognized and measured at fair value, the value should include the value of the intangible assets to be used in a particular research and development project.

Question 11 – Do you agree with the proposed accounting for business combinations in which the consideration transferred for the acquirer’s interest in the acquiree is less than the fair value of that interest? If not, what alternative do you propose and why?

We agree with the Board’s proposed accounting for business combinations in which the consideration transferred for the acquirer’s interest in the acquiree is less than the fair value of that interest (bargain purchase). Paragraph 61 states that if a business combination is a bargain purchase, then the acquirer shall account for the excess by first reducing the amount of goodwill that otherwise would be recognized. Then, if goodwill is reduced to zero, the remaining excess would be recognized as a gain. While we believe that the accounting theory behind this is appropriate, we do not feel it is worthwhile from a cost/benefit perspective to expect the acquirer to follow all of the steps outlined in the EEJ. In the example provided in paragraphs A64-A66, the EEJ states that an independent third party is to be hired by the acquirer’s management to determine the fair value of the acquiree by using multiple valuation techniques. Results of the independent valuation study are later used to calculate the goodwill amount to be tentatively recognized and adjusted “gain” on bargain purchase for any excess remaining after reducing goodwill to zero. As shown by the second example, the same result can be calculated by simply taking the difference of fair value of the consideration transferred and net

(2) Costs Associated with Exit or Disposal Activities By Robert A. Young, CFA Journal, December 2001
(3) SEC Sensity of In-Process Research and Development Deloitte & Touche Review, December 21, 1992
amount of the fair value of the separately recognized identifiable assets. Given the alternative, we feel that it would be more practical and cost-efficient for most acquirers to avoid hiring an independent third party firm and use the second calculation method instead.

Question 14 - Do you believe that the guidance provided is sufficient for making the assessment of whether any portion of the transaction price or any assets acquired and liabilities assumed or incurred are not part of the exchange for the acquiree? If not, what other guidance is needed?

We agree that the Board provided sufficient information to assess whether or not these items should be included in the exchange and reasons for the exclusion. We also believe that the extensive guidelines and discussion on employee-based compensation and share-based pay is sufficient to make a determination if it is to be excluded from the exchange. We believe the description, discussion, and examples provided in the ED give sufficient guidance to determine if any portion of the transaction is not part of the exchange.

We appreciate the opportunity to comment on the ED and hope the response contained in this letter will be helpful during the Board's deliberation of this issue.

Respectfully,

MPA Students (Corporate Financial Reporting)
Indiana University Kelley School of Business Indianapolis

Ryan Hammons
Meranda Hillock
Kent Kelley
Irina N. Nix
Jia Zhang