MINUTES

Financial Accounting Standards Board

To: Board Members

From: Business Combinations—Purchase Method Procedures Team (Wilson, ext. 275)

Subject: Revised Minutes of the February 26, 2003 Board Meeting

Date: February 28, 2003

cc: FASB: Bielstein, Smith, Petrone, Bossio, Tamulis, Munro, Manders, B. Wilson, Swift, Polley, Cropsey, Thompson, Gabriele, Sutay, Lapolla, FASB Intranet; IASB: Leisenring, Ryltsova, Kimmitt; CICA: Walsh; AICPA: Hekker; Purchase Method Procedures Working Group Members

Topic: Business Combinations—Purchase Method Procedures: Control Obtained (or Lost) Through Means Other Than an Acquisition (or Disposition) of Net Assets That Constitute a Business or Equity Instruments

Basis for Discussion: Memorandum dated February 10, 2003

Length of Discussion: Starting Time: 9:00 a.m. Concluding Time: 10:30 a.m.

Attendance:

Board members present:	FASB: Herz, Crooch, Foster, Trott, Schieneman, Schipper, Wulff IASB: Leisenring
Board members absent:	None
Staff in charge of topic:	Tamulis,
Other staff at Board table:	Bielstein, Bossio, Manders, Wilson
Outside participants:	Ryltsova (by phone)

Summary for ACTION ALERT:

The Board decided to amend the definition of a business combination in FASB Statement No. 141, *Business Combinations,* to include events and circumstances in which an entity obtains control over a business through means other than a transaction involving an acquisition of the net assets or equity interests in that business.

The Board discussed the impact of amending the definition of a business combination on joint ventures, entities under common control, and variable interest entities (VIEs) subject to the provisions of FASB Interpretation No. 46, *Consolidation of Variable Interest Entities*. The Board noted that, as in Statement 141, the scope of a proposed Statement on business combinations would continue to exclude from its scope the formation of a joint venture or transactions between entities under common control. Under Interpretation 46, newly consolidated VIEs are not subject to the initial measurement requirements of Statement 141. Since the Board has decided to amend the definition of a business combination to include events and circumstances in which control is obtained through other means, the Board decided to amend Interpretation 46 such that if a newly consolidated VIE meets the definition of a business as defined in EITF Issue No. 98-3 "Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business," an event resulting in obtaining control of that VIE would be in the scope of this joint project.

The Board also discussed the issue of losing control of a subsidiary through means other than a sale of the subsidiary's net assets or equity instruments. The Board decided that, consistent with its tentative decisions for derecognition of a subsidiary when control is lost through a sale of ownership interests, the gain or loss on the derecognition of a subsidiary when control is lost through other means should be recognized in the income statement for that period and calculated as the difference between:

a. The carrying amount of the subsidiary's net assets in the consolidated financial statements at the date control is lost

b. The sum of the carrying amount of any noncontrolling interest in the subsidiary and the fair value of any investment remaining in the former subsidiary.

Matters Discussed and Decisions Reached:

The Board discussed whether to amend the definition of a business combination in Statement 141. The staff noted that the definition of Statement 141 is not as broad as the definition in the IASB's Exposure Draft 3, *Business Combinations* (ED 3) and IAS 22, *Business Combinations*. The staff also noted that the difference between the FASB's and IASB's definitions might result in similar events being accounted for as a business combination under international guidance, but not under U.S. GAAP. The staff recommended that as part of this joint project that the FASB amend its definition of a business combination to include transactions or events which an entity obtains control of a business without the acquisition of its net assets or its equity instrument, which would result in a scope similar to that of the IASB. All of the Board members supported the recommendation to broaden the definition of a business combination in Statement 141.
Some Board members questioned why the words proposed by the staff for the amended definition would not be the same as the definition proposed in the IASB's ED 3. It was noted that that could leave room for different interpretations about whether a particular transaction or event is a business combination. The staff stated that although they had considered using the definition in ED 3, the staff did not recommend that definition for two reasons. The first reason was because the IASB's definition does not focus on the notion of control being the event that would result in a business combination, whereas the definition proposed by the staff does. This is because the IASB's definition is broad enough to leave open the possibility of a "true merger" or a "merger of equals." In Statement 141, the FASB decided that true mergers do not exist or are so rare that separate accounting is not warranted for them. The second reason is that the IASB's definition uses the words "separate entities' or "operations of entities," which are not defined in international or U.S. guidance. The FASB's definition uses the word "business," which is defined in U.S. guidance but not international guidance, so the staff suggested retaining the word business in its definition. The Board agreed to amend the definition of a business combination as proposed by the staff. [6 Board members agreed; 1 did not: RHH] Mr. Herz noted that Board members prefer the definition recommended by the staff but asked that the staff seek to learn whether there might be opportunities for the FASB and IASB to agree on the same definition of a business combination.

The Board discussed the impact of amending the definition of a business combination on joint ventures, entities under common control, and VIEs subject to the provisions of FASB Interpretation 46. The staff noted that the scope of a proposed Statement on business combinations would continue to exclude from its scope the formation of a joint venture or transactions between entities under common control. The staff also noted that currently a VIE is not subject to Statement 141 primarily because Statement 141 does not address transactions in which control of a business is obtained through means other than an acquisition of its net assets or its equity interests. A primary beneficiary of a VIE generally does not obtain control through a purchase of equity interests or net assets. The staff had recommended that VIEs be excluded from the scope of the business combinations standard and that the guidance in Interpretation 46 for initial measurement of a newly consolidated VIE would continue to apply. The staff also noted that during our educational meeting a Board member suggested that if the Board decides to amend the definition of a business combination to include events and circumstances in which control is obtained through other means, such as a newly consolidated VIE that meets the definition of a business as defined in Issue 98-3, an event resulting in obtaining control of that VIE should be in the scope of this joint project. The Board discussed whether a VIE could also be a business as defined in Issue 98-3, and agreed that it is possible that a VIE could meet the definition of a business. (Some Board members observed, however, that that would not be a frequent or common occurrence.) The Board agreed with the suggestion and decided to amend Interpretation 46 such that if a newly consolidated VIE meets the definition of a business as defined in Issue 98-3, an event resulting in obtaining control of that VIE would be in the scope of this joint project. [All Board members agreed]

The Board also discussed the issue of losing control of a subsidiary through means other than a sale or disposition of the subsidiary's net assets or equity instruments. The Board decided that the accounting should be consistent with its tentative decisions for derecognition of a subsidiary when control is lost through a sale of ownership interests and, thus, the gain or loss on the loss of control should be recognized in the income statement for that period, and calculated as the difference between (1) the carrying amount of the subsidiary's net assets in the consolidated financial statements at the date control is lost and (2) the sum of the carrying amount of any noncontrolling interest in the subsidiary and the fair value of any investment remaining in the former subsidiary. [5 Board members agreed; 2 did not: JMF, GMC] Subsequent to the meeting, Mr. Foster advised that he needed more time to consider his position. He noted that he might support the recommendation on the basis that removing noncontrolling interest from equity at its carrying amount is similar to a distribution of equity to shareholders.

Follow-up Items:

None

General Announcements:

None