MINUTES

Financial Accounting Standards Board

To: Board Members

From: Convergence—Income Tax Team
(Beckendorff, Ext. 229)

Subject: Minutes of the January 31, 2007 Board Meeting

Date: February 7, 2007

cc: Bielstein, Smith, MacDonald, Lott, Convergence Income Tax Project Team (Beckendorff, Cassel, Cowan, Kosminoff, Paul, Posta, Rhine), Business Combinations Project Team (Bossio, Delmonico, Tamulis, Vessels, Willis), Allen, Beswick, Gabriele, Carney, Polley, Chookaszian, Glotzer, Tully, Sutay, FASB Intranet, IASB: Buschhueter, Eastman, Leisenring, Hickey, Kwiatkawska, Maybin, McGeachin, Teixiera, Quiring, Upton,

Topic: Issues Related to Business Combinations

Basis for Discussion: Board Memorandum 17 dated January 17, 2007

Length of Discussion: 9:00 a.m. to 9:10 a.m. (EST)

Attendance:

Board members present: FASB: Herz, Trott, Linsmeier, Batavick, Crooch, Seidman, and Young
IASB: Leisenring

Board members absent: None

Staff in charge of topic: Paul, Posta

Other staff at Board table: Tamulis, Cassel, Rhine, Beckendorff, Bielstein

IASB Phone Participants: Buschhuter, Kwiatkowska, McGeachin,Teixeira

Outside participants: None

Summary of Decisions Reached:

The Board decided:

1. To require that an asset acquired with a tax basis difference be recorded at fair value rather than fair value (assuming full deductibility for tax purposes). This decision clarifies the Board's previous decision from the April 2004 Joint meeting. In that meeting, the Boards' had tentatively concluded that when a temporary difference is acquired in an asset acquisition, then (a) the asset should be recognized at fair value (assuming full deductibility for tax purposes), (b) the corresponding deferred tax asset or liability should be recognized as the difference between the fair value of the asset and its tax basis multiplied by the tax rate, and (c) any difference between the consideration paid and the sum of the fair value of the asset and the recognized deferred tax amount is recognized as a purchase discount allowance on the deferred tax.
2. To retain the guidance in FASB Statement No. 109, *Accounting for Income Taxes*, by continuing to prohibit the recognition of a deferred tax liability for the portion of goodwill for which amortization is not deductible for tax purposes.

Objective of Meeting:

The objective of the meeting was for the Board to reach decisions on two income tax issues related to business combinations: (1) Whether to clarify the tentative decision to record the acquisition of an asset with a tax basis difference at fair value (assuming full deductibility for tax purposes)? and (2) whether to retain the guidance in Statement 109 by continuing to prohibit the recognition of a deferred tax liability for the amount of goodwill that is not deductible for tax purposes. The objective was met. [The Board discussed other issues related to the accounting for income taxes in a business combinations at today's meeting.]

Matters Discussed and Decisions Reached:

Issue 1: Recording the acquisition of an asset with a tax basis difference at fair value.

1. Mr. Paul stated that the first issue is whether the Board wishes to refine the joint tentative decision for acquired temporary differences in asset acquisitions outside of a business combination and whether the asset should be recorded at fair value, or fair value (assuming full deductibility for tax purposes). He noted that the minutes and action alert from the previous joint meeting in April of 2004 stated that the asset acquired would be recorded at fair value (assuming full deductibility for

tax purposes). He stated that the staff has provided hypothetical examples of situations when the amount recorded under that guidance would be different than fair value and, therefore, requests that the Board clarify if such assets should be measured at (a) Fair value, or (b) Fair value (assuming full deductibility for tax purposes). Mr. Paul stated that the staff recommends the first alternative, fair value.

2. Mr. Paul noted that subsequent to the issuance of Memorandum 17, IASB advisory members indicated that they would prefer that assets acquired with temporary differences be measured at fair value. The IASB staff will also ask the IASB to clarify its intention.

3. All Board members agreed that fair value was the proper alternative for measuring an asset acquired with a tax basis difference. Mr. Herz noted that he believes the FASB had always intended the use of fair value. Mr. Leisenring added that the parenthetical note was simply to clarify that the asset should not be recorded net of taxes.

Issue 2: Recognition of deferred tax liabilities for the amount of goodwill that is not deductible for tax purposes.

4. Ms. Posta stated that current requirements in Statement 109 and IAS 12 prohibit the recognition of a deferred tax liability for the amount of goodwill that is not deductible for tax purposes.

5. Ms. Posta stated that the IASB revisited that requirement within this project and tentatively concluded to remove that exception. The IASB plans to revisit that decision after it concludes on the recognition of goodwill in a less than 100 percent acquisition. She stated that the IASB is in the process of considering the recognition of goodwill in a business combination. Therefore, depending on the outcome of its deliberations on goodwill, as well as the FASB's decisions in this meeting, the IASB staff plans to bring this issue back to the IASB for reconsideration.

6. Ms. Posta stated that Board members discussed this issue in small group meetings in November 2006. In those meetings, Board members weighed the

relative merits associated with retaining and eliminating the exception for nondeductible goodwill in terms of the relevance to users of financial statements, symmetry between deferred tax assets and liabilities for goodwill, consistency with the principles of Statement 109, complexity of calculation at the acquisition date, and complexity of the accounting post acquisition. She stated that during those meetings, Board members expressed a preliminary preference to retain the existing guidance in Statement 109. Ms. Posta stated that the Board memo on this issue summarizes the input from those small group meetings and asks whether the Board supports:

a. Retaining the existing guidance in Statement 109 for purposes of the forthcoming Exposure Draft on the convergence income taxes project (Alternative A), or

b. Further exploring the elimination of the exception for nondeductible goodwill as part of the convergence income taxes project (Alternative B).

7. Ms. Posta stated that one staff member supports Alternative B and believes that the Boards should be consistent with the principles of the temporary difference approach, consistent in the treatment of deferred tax assets and liabilities, and consistent with the treatment of other nonamortized intangibles. However, on balance, in considering the relevance, potential complexity, and the scope of the project; the staff recommends that the Board retain the guidance in Statement 109 by continuing to prohibit the recognition of deferred tax liabilities for nondeductible goodwill (Alternative A).

8. Mr. Herz asked whether any Board member favored changing the existing guidance. No Board member favored changing the existing guidance.

9. Mr. Herz stated that even though he does not support providing deferred tax liabilities for nondeductible goodwill, he wanted to raise an issue in the context of the debate over the recognition of full versus partial goodwill in an acquisition of less than 100 percent of an acquiree. He stated that, if the Boards require the recognition of full goodwill, most jurisdictions will not allow a tax basis for the imputed step up on the goodwill related to the noncontrolling interest. He stated that there may be implications with existing accounting which only recognizes

goodwill on the acquired portion, and he mentioned that this may be one of the issues that the IASB staff will explore.

Follow-up Items:

Based on the issue raised by Mr. Herz, the staff plans to further research possible income tax issues associated with the changes for the accounting for noncontrolling ownership interests that were proposed in the Business Combinations Project.

General Announcements:

None.