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Preface

October 2017

To our friends and clients:

We are pleased to present A Roadmap to Accounting for Asset Acquisitions. This Roadmap provides Deloitte’s insights into and interpretations of the guidance on accounting for an acquisition of an asset, or a group of assets, that does not meet the U.S. GAAP definition of a business in ASC 805-10.

The body of this Roadmap combines the principles from the “Acquisition of Assets Rather Than a Business” subsections of ASC 805-50 with Deloitte’s interpretations and examples in a comprehensive, reader-friendly format. Further, the table of contents is a helpful navigational tool, providing links to topics and interpretations.

We intend to incorporate this Roadmap — along with the others covering additional business combinations issues addressed in subsections of ASC 805-50 — into a comprehensive business combinations Roadmap in the future.

Subscribers to the Deloitte Accounting Research Tool (DART) may access any interim updates to this publication by selecting the document from the “Roadmaps” tab on DART’s home page. If a “Summary of Changes Since Issuance” displays, subscribers can view those changes by clicking the related links or by opening the “active” version of the Roadmap.

We hope that you find this publication a valuable resource when considering the guidance on accounting for asset acquisitions.

Sincerely,

Deloitte & Touche LLP
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Accounting for Asset Acquisitions

AA.1 Overview and Scope

The term “asset acquisition” is used to describe an acquisition of an asset, or a group of assets, that does not meet the U.S. GAAP definition of a business in ASC 805-10. An asset acquisition may also involve the assumption of liabilities. An asset acquisition is accounted for in accordance with the “Acquisition of Assets Rather Than a Business” subsections of ASC 805-50 by using a cost accumulation model. In a cost accumulation model, the cost of the acquisition, including certain transaction costs, is allocated to the assets acquired on the basis of relative fair values. In contrast, a business combination is accounted for by using a fair value model under which the assets and liabilities are generally recognized at their fair values and the difference between the consideration transferred, excluding transaction costs, and the fair values of the assets and liabilities is recognized as goodwill. As a result, there are significant differences between the accounting for an asset acquisition and the accounting for a business combination.

Changing Lanes

As of the date of this publication, the FASB has a project on its agenda to address differences between the accounting for acquisitions of assets and that for business combinations. On its project update page, the FASB indicates that the project is focusing on whether certain differences within the acquisition models can be aligned, “specifically the accounting for transaction costs, in process research and development (IPR&D), and contingent consideration.” The FASB may also “consider whether certain exceptions in the accounting for business combinations should be extended to the accounting for acquisitions of assets, including the reassessment of certain contracts (such as leases) and the measurement exceptions associated with reacquired rights, indemnification assets, and leases.”

1 For a list of the titles of standards and other literature referred to in this publication, see Appendix B. For a list of abbreviations used in this publication, see Appendix C.
## AA.1.1 Summary of Significant Differences Between the Accounting for a Business Combination and the Accounting for an Asset Acquisition

The table below summarizes the significant differences between the accounting for an asset acquisition and that for a business combination. Each of these differences is described in further detail in later sections.

<table>
<thead>
<tr>
<th>Issue</th>
<th>Accounting in a Business Combination</th>
<th>Accounting in an Asset Acquisition</th>
</tr>
</thead>
<tbody>
<tr>
<td>General principle</td>
<td>Fair value model: assets and liabilities are recognized at fair value, with certain exceptions.</td>
<td>Cost accumulation model: the cost of the acquisition, including most transaction costs, is allocated to the assets, with certain exceptions, on the basis of relative fair values. This allocation results in the recognition of some assets at other than their fair values (see Section AA.1).</td>
</tr>
<tr>
<td>Scope</td>
<td>Acquisition of a business as defined in ASC 805-10.</td>
<td>Acquisition of an asset or a group of assets (and liabilities) that does not constitute a business as defined in ASC 805-10 (see Section AA.1.2).</td>
</tr>
<tr>
<td>Acquisition-related costs or transaction costs</td>
<td>Acquisition-related costs are expensed as incurred, except for costs of issuing debt and equity securities, which are accounted for under other GAAP.</td>
<td>Transaction costs are included in the cost of the acquisition, except for costs of issuing debt and equity securities, which are accounted for under other GAAP. Indirect costs are expensed as incurred (see Section AA.2.1.1).</td>
</tr>
<tr>
<td>Contingent consideration</td>
<td>Recognized at fair value and classified as a liability, equity, or an asset on the acquisition date on the basis of the terms of the arrangement. Subsequently, any changes in the fair value of contingent consideration classified as a liability or as an asset are recognized in earnings until they are settled.</td>
<td>Recognized at fair value under ASC 815 if a derivative, under ASC 450 when it becomes probable and reasonably estimable, or by analogy to ASC 323-10 (see Section AA.2.1.2).</td>
</tr>
<tr>
<td>Goodwill</td>
<td>Recognized as the difference between (1) the sum of the consideration transferred, the fair value of any noncontrolling interests, and the fair value of any previously held interests and (2) the identifiable assets acquired and liabilities assumed.</td>
<td>Not recognized. Any excess of the cost of the acquisition over the fair value of the net assets acquired is allocated to certain assets on the basis of relative fair values (see Section AA.3).</td>
</tr>
<tr>
<td>Bargain purchases</td>
<td>Recognized as a gain on the acquisition date.</td>
<td>Not recognized. Any excess of the fair value of the net assets acquired over the cost of the acquisition is allocated to certain assets on the basis of relative fair values (see Section AA.3).</td>
</tr>
<tr>
<td>Contingencies</td>
<td>Measured at fair value, if determinable; otherwise, measured at their estimated amounts if probable and reasonably estimable. If such assets or liabilities cannot be measured during the measurement period, they are accounted for separately from the business combination in accordance with other GAAP, such as ASC 450.</td>
<td>Accounted for in accordance with ASC 450 on the acquisition date and subsequently. Loss contingencies are recognized when they are probable and reasonably estimable. Gain contingencies are recognized when realized and are thus not recognizable in an asset acquisition (see Section AA.3.2).</td>
</tr>
</tbody>
</table>
**Accounting for Asset Acquisitions**

<table>
<thead>
<tr>
<th>Issue</th>
<th>Accounting in a Business Combination</th>
<th>Accounting in an Asset Acquisition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intangible assets</td>
<td>Recognized at fair value if they are identifiable (i.e., if they are separable or arise from contractual rights).</td>
<td>Recognized on the basis of relative fair value under ASC 350-10 if they meet the asset recognition criteria in FASB Concepts Statement 5 (see Section AA.3.4).</td>
</tr>
<tr>
<td>Assembled workforce</td>
<td>Not recognized because it is presumed not to be identifiable.</td>
<td>Recognized because it is presumed to meet the asset recognition criteria in FASB Concepts Statement 5. However, the presence of an assembled workforce may indicate that the acquisition is a business combination rather than an asset acquisition (see Section AA.3.4.1).</td>
</tr>
<tr>
<td>IPR&amp;D</td>
<td>Measured at fair value and recognized as an indefinite-lived intangible asset until completion or abandonment of the related project, then reclassified as a finite-lived intangible asset and amortized.</td>
<td>Expensed under ASC 730 unless the IPR&amp;D has an alternative future use (see Section AA.3.4.2).</td>
</tr>
<tr>
<td>Deferred taxes</td>
<td>Generally recognized for most temporary book/tax differences related to assets acquired and liabilities assumed under ASC 740.</td>
<td>Generally recognized for temporary book/tax differences in an asset acquisition by using the simultaneous equations method in accordance with ASC 740 (see Section AA.3.5).</td>
</tr>
<tr>
<td>Lease classification</td>
<td>Classification of a lease contract is not reassessed in a business combination unless the lease contract has been significantly modified.</td>
<td>Classification of a lease contract is reassessed by the lessee in an asset acquisition (see Section AA.3.6).</td>
</tr>
<tr>
<td>Measurement period</td>
<td>The acquirer has a defined period under ASC 805 after the acquisition date to identify and measure the consideration transferred, the assets acquired, and the liabilities assumed. This period might extend beyond the next reporting date.</td>
<td>No concept of a measurement period. All assets acquired (and liabilities assumed) must be measured by the next reporting date (see Section AA.3.8).</td>
</tr>
</tbody>
</table>

**SEC Considerations**

A registrant must also consider certain SEC reporting requirements when it acquires an asset or a group of assets. For instance, the registrant must separately evaluate whether the asset or group of assets meets the definition of a business for SEC reporting purposes under SEC Regulation S-X, Rule 11-01(d), since this definition differs from the U.S. GAAP definition of a business under ASC 805-10. The SEC reporting requirements for an asset acquisition are addressed in Section AA.5.
AA.1.2 Scope

The guidance in the "Acquisition of Assets Rather Than a Business" subsections of ASC 805-50 applies to the acquisition of an asset (or group of assets) and the assumption of any liabilities that do not meet the definition of a business in ASC 805-10. As a result, entities first need to assess whether the assets acquired and any liabilities assumed meet the definition of a business by applying the guidance in ASC 805-10.

Changing Lanes

On January 5, 2017, the FASB issued ASU 2017-01 to clarify the definition of a business in ASC 805-10. The FASB issued the ASU in response to stakeholder feedback that the definition of a business was being applied too broadly. In addition, stakeholders said that analyzing transactions under the current definition is difficult and costly. The Background Information and Basis for Conclusions indicates that the amendments “narrow the definition of a business and provide a framework that gives entities a basis for making reasonable judgments about whether a transaction involves an asset or a business.”

ASU 2017-01 is effective for public business entities for annual periods beginning after December 15, 2017, including interim periods therein. For all other entities, the ASU is effective for annual periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. The ASU must be applied prospectively on or after the effective date. Early adoption is permitted for transactions (i.e., acquisitions or dispositions) that occurred before the issuance date or effective date of the standard if the transactions were not reported in financial statements that have been issued or made available for issuance.

The definition of a business for SEC reporting purposes in SEC Regulation S-X, Rule 11-01(d), and used by registrants to determine when financial statements and pro forma information are needed in SEC filings is different from the definition for U.S. GAAP accounting purposes. The SEC has not changed this definition as a result of the ASU's amendments. See Section AA.5.2 for more information.
5

AA.1.2.1 Scope Exception for Variable Interest Entities

ASC 805-10-15-4 states that the “Acquisition of Assets Rather Than a Business” subsections of ASC 805-50 do not apply to the initial consolidation of a VIE whose assets and liabilities do not meet the definition of a business in ASC 805-10. ASC 810-10-30-3 and 30-4 provide guidance on such acquisitions.

ASC 810-10

30-3 When a reporting entity becomes the primary beneficiary of a VIE that is not a business, no goodwill shall be recognized. The primary beneficiary initially shall measure and recognize the assets (except for goodwill) and liabilities of the VIE in accordance with Sections 805-20-25 and 805-20-30. However, the primary beneficiary initially shall measure assets and liabilities that it has transferred to that VIE at, after, or shortly before the date that the reporting entity became the primary beneficiary at the same amounts at which the assets and liabilities would have been measured if they had not been transferred. No gain or loss shall be recognized because of such transfers.

30-4 The primary beneficiary of a VIE that is not a business shall recognize a gain or loss for the difference between (a) and (b):
   a. The sum of:
      1. The fair value of any consideration paid
      2. The fair value of any noncontrolling interests
      3. The reported amount of any previously held interests
   b. The net amount of the VIE’s identifiable assets and liabilities recognized and measured in accordance with Topic 805.

The primary beneficiary of a VIE that does not meet the definition of a business should initially measure and recognize the assets and liabilities of the VIE in accordance with ASC 805-20-25 and ASC 805-20-30 but should not recognize goodwill. Because goodwill is not recognized, the primary beneficiary recognizes a gain or loss calculated on the basis of the requirements in ASC 810-10-30-4. The primary beneficiary recognizes the identifiable assets acquired (excluding goodwill), the liabilities assumed, and any noncontrolling interests as though the VIE was a business and subject to the guidance on recognition and measurement in a business combination. As a result, the assets acquired (excluding goodwill), liabilities assumed, and any noncontrolling interests are measured and recognized the same way as they would be in a business combination. IPR&D and contingent consideration therefore would be recognized at fair value upon acquisition, and the applicable recognition and fair value measurement exceptions would be the same as those for a business combination.

However, to prevent the improper recognition of gains or losses resulting from transfers of assets and liabilities to VIEs, the FASB developed the guidance in ASC 810-10-30-3. Under this guidance, assets and liabilities that a legal entity transfers to a VIE that is not a business “at, after, or shortly before the date that the . . . entity became the [VIE’s] primary beneficiary [should be measured] at the same amounts at which the assets and liabilities would have been measured if they had not been transferred.” In addition, under ASC 810-10-30-4, if the VIE is acquired in stages (i.e., step acquisition), the reported amount of the previously held interest must be used to calculate the gain or loss.

A legal entity’s failure to meet the business scope exception in ASC 810-10-15-17(d) does not mean that the legal entity does not qualify as a business under ASC 805-10. The determination of whether a legal entity is a business under ASC 810-10-30-2 is strictly related to whether the legal entity qualifies as a business under ASC 805-10. That is, even if the business scope exception is not applicable because one or more of the four additional conditions in that paragraph are met, as long as the definition of a business in ASC 805-10 is met, goodwill, if any, should be recorded. See Deloitte’s A Roadmap to
Consolidation — Identifying a Controlling Financial Interest for more information about the business scope exception.

AA.2  Measuring the Cost of an Asset Acquisition

**ASC 805-50**

**Acquisition Date Recognition of Consideration Exchanged**

25-1 Assets commonly are acquired in exchange transactions that trigger the initial recognition of the assets acquired and any liabilities assumed. If the consideration given in exchange for the assets (or net assets) acquired is in the form of assets surrendered (such as cash), the assets surrendered shall be derecognized at the date of acquisition. If the consideration given is in the form of liabilities incurred or equity interests issued, the liabilities incurred and equity interests issued shall be initially recognized at the date of acquisition.

**Pending Content (Transition Guidance: ASC 606-10-65-1)**

25-1 Assets commonly are acquired in exchange transactions that trigger the initial recognition of the assets acquired and any liabilities assumed. If the consideration given in exchange for the assets (or net assets) acquired is in the form of assets surrendered (such as cash), the assets surrendered shall be derecognized at the date of acquisition. If the consideration given is in the form of liabilities incurred or equity interests issued, the liabilities incurred and equity interests issued shall be initially recognized at the date of acquisition. However, if the assets surrendered are nonfinancial assets or in substance nonfinancial assets within the scope of Subtopic 610-20 on gains and losses from the derecognition of nonfinancial assets, the assets surrendered shall be derecognized in accordance with the guidance in Subtopic 610-20 and the assets acquired shall be treated as noncash consideration in accordance with Subtopic 610-20.

**Determining Cost**

30-1 Paragraph 805-50-25-1 discusses exchange transactions that trigger the initial recognition of assets acquired and liabilities assumed. Assets are recognized based on their cost to the acquiring entity, which generally includes the transaction costs of the asset acquisition, and no gain or loss is recognized unless the fair value of noncash assets given as consideration differs from the assets' carrying amounts on the acquiring entity's books. For transactions involving nonmonetary consideration within the scope of Topic 845, an acquirer must first determine if any of the conditions in paragraph 845-10-30-3 apply.

**Pending Content (Transition Guidance: ASC 606-10-65-1)**

30-1 Paragraph 805-50-25-1 discusses exchange transactions that trigger the initial recognition of assets acquired and liabilities assumed. Assets are recognized based on their cost to the acquiring entity, which generally includes the transaction costs of the asset acquisition, and no gain or loss is recognized unless the fair value of noncash assets given as consideration differs from the assets' carrying amounts on the acquiring entity's books. For transactions involving nonmonetary consideration within the scope of Topic 845, an acquirer must first determine if any of the conditions in paragraph 845-10-30-3 apply. If the consideration given is nonfinancial assets or in substance nonfinancial assets within the scope of Subtopic 610-20 on gains and losses from the derecognition of nonfinancial assets, the assets acquired shall be treated as noncash consideration and any gain or loss shall be recognized in accordance with Subtopic 610-20.
Asset acquisitions in which the consideration given is cash are measured by the amount of cash paid, which generally includes the transaction costs of the asset acquisition. However, if the consideration given is not in the form of cash (that is, in the form of noncash assets, liabilities incurred, or equity interests issued), measurement is based on either the cost which shall be measured based on the fair value of the consideration given or the fair value of the assets (or net assets) acquired, whichever is more clearly evident and, thus, more reliably measurable. For transactions involving nonmonetary consideration within the scope of Topic 845, an acquirer must first determine if any of the conditions in paragraph 845-10-30-3 apply.

Pending Content (Transition Guidance: ASC 606-10-65-1)

30-2 Asset acquisitions in which the consideration given is cash are measured by the amount of cash paid, which generally includes the transaction costs of the asset acquisition. However, if the consideration given is not in the form of cash (that is, in the form of noncash assets, liabilities incurred, or equity interests issued), measurement is based on either the cost which shall be measured based on the fair value of the consideration given or the fair value of the assets (or net assets) acquired, whichever is more clearly evident and, thus, more reliably measurable. For transactions involving nonmonetary consideration within the scope of Topic 845, an acquirer must first determine if any of the conditions in paragraph 845-10-30-3 apply. If the consideration given is nonfinancial assets or in substance nonfinancial assets within the scope of Subtopic 610-20, the assets acquired shall be treated as noncash consideration and any gain or loss shall be recognized in accordance with Subtopic 610-20.

AA.2.1 General Principles for Measuring the Cost of an Asset Acquisition

The “Acquisition of Assets Rather Than a Business” subsections of ASC 805-50 provide general principles (discussed in this section) for measuring the cost of an asset acquisition. This guidance applies when the asset acquisition is not within the scope of other GAAP.

An asset acquisition is an exchange transaction that triggers the acquiring entity’s initial recognition of any assets acquired or liabilities assumed and the derecognition of any consideration given on the date of the acquisition. The consideration given may be in the form of cash, other assets, equity interests, or liabilities incurred (e.g., contingent consideration).

If the consideration given is in cash, measurement is based on the amount of cash the acquiring entity pays. For an asset acquisition that is within the scope of ASC 805-50, if the consideration given includes noncash assets, liabilities incurred, or equity interests issued, the assets acquired are measured by using either the cost to the acquiring entity or the fair value of the net assets acquired, whichever is more reliably measurable. In measuring the fair value of the consideration given (and the fair value of the net assets acquired), the acquiring entity applies the guidance in ASC 820. The cost of an asset acquisition is presumed to equal the fair value of the net assets acquired. Therefore, the acquiring entity recognizes no gain or loss on the date of acquisition unless the consideration given consists of noncash assets whose fair value differs from their carrying amounts. In that case, the acquiring entity recognizes a gain or loss at the time of the acquisition to remeasure those noncash assets at fair value. However, ASC 805-50 specifies that when an asset acquisition is within the scope of other GAAP, such as ASC 845 on nonmonetary transactions or ASC 610-20 on nonfinancial assets (once effective), an entity would apply that guidance rather than the general principles in ASC 805-50. For more information, see Sections AA.2.2 and AA.2.3 of this Roadmap.

A significant difference between the cost of an asset acquisition and the fair value of the net assets acquired may indicate that not all of the assets acquired or liabilities assumed have been recognized or that the cost of the asset acquisition includes a payment for something other than the acquired net assets that should be accounted for separately from the asset acquisition (see Section AA.2.4).
AA.2.1.1 Transaction Costs, Including Costs of Issuing Debt or Equity Securities

ASC 805-50-30-1 states that, in an asset acquisition, “[a]ssets are recognized based on their cost to the acquiring entity, which generally includes the transaction costs.” ASC 805-50 does not, however, define transaction costs. We believe that transaction costs should be limited to the direct and incremental costs incurred to complete the asset acquisition, such as third-party costs for finders’ fees and advisory, legal, accounting, valuation, and other professional or consulting fees. Costs such as general and administrative costs and salaries and benefits of the acquiring entity’s employees working on the acquisition should not be considered transaction costs.

We also believe that the acquiring entity should recognize the costs of issuing debt or equity securities in an asset acquisition in accordance with applicable GAAP, which is the same way those costs are recognized in a business combination. SEC SAB Topic 5.A provides guidance on accounting for the costs of issuing equity securities and states, in part, that “[s]pecific incremental costs directly attributable to a proposed or actual offering of securities may properly be deferred and charged against the gross proceeds of the offering.” Therefore, the costs of issuing equity securities are generally reflected as a reduction of the amount that would have otherwise been recognized in additional paid-in capital.

If the acquiring entity incurs debt to fund the asset acquisition, it should present the debt issuance costs in the balance sheet as a direct deduction from the face amount of the debt and amortize them as interest expense in accordance with ASC 835-30-45 (unless the debt financing is from a revolving arrangement, in which case the acquiring entity can elect to either deduct the costs from the drawn balance or recognize them as an asset).

AA.2.1.2 Contingent Consideration

The ASC master glossary defines “contingent consideration” as follows:

Usually an obligation of the acquirer to transfer additional assets or equity interests to the former owners of an acquiree as part of the exchange for control of the acquiree if specified future events occur or conditions are met. However, contingent consideration also may give the acquirer the right to the return of previously transferred consideration if specified conditions are met.

While that definition applies to contingent consideration issued in a business combination, contingent consideration may also be issued in an asset acquisition. The acquiring entity should assess the terms of the transaction to determine whether consideration payable at a future date is contingent consideration or seller financing. If the payment depends on the occurrence of a specified future event or the meeting of a condition and the event or condition is substantive, the additional consideration should be accounted for as contingent consideration. If the additional payment depends only on the passage of time or is based on a future event or the meeting of a condition that is not substantive, the arrangement should be accounted for as seller financing.

ASC 805-50 states only that any liabilities incurred by the acquiring entity are part of the cost of the asset acquisition; it does not provide any specific guidance on accounting for contingent consideration in an asset acquisition. However, in EITF Issue 09-2, the Task Force addressed contingent consideration in an asset acquisition. While a final consensus was not reached, the minutes from the September 9–10, 2009, EITF meeting state that “the Task Force reached a consensus-for-exposure that contingent consideration in an asset acquisition shall be accounted for in accordance with existing U.S. GAAP” as follows:

• ASC 815 requires recognition of “contingent consideration [that meets] the definition of a derivative” at fair value.

• ASC 450 may “require recognition of [a liability for] contingent consideration if it is probable that a liability has been incurred and the amount of that liability can be reasonably estimated.”
• ASC 323-10 “may require the recognition of the contingent consideration if it relates to the acquisition of an investment that is accounted for under the equity method.”

The minutes also state that when contingent consideration related to an asset acquisition is recognized at inception, “such [an] amount would be included in the initial measurement of the cost of the acquired assets.”

If not recognized initially, contingent consideration that is accounted for in accordance with ASC 450 may be recognized at a later date. If the acquirer recognizes a liability for a contingent payment after the date of acquisition, that amount is capitalized as part of the cost of the assets acquired and is allocated to increase the eligible assets on a relative fair value basis. (However, any portion of a contingent payment that is related to IPR&D assets with no alternative future use should be immediately expensed.) Similarly, we believe that if the acquiring entity receives a payment from the seller for the return of previously transferred consideration when certain conditions are met (i.e., a contingent consideration asset), the entity should allocate that amount to reduce the eligible assets on a relative fair value basis. In addition, when contingent consideration is recognized at a later date in accordance with ASC 450, the value of an amortizable or depreciable identifiable asset may be adjusted (e.g., property, plant, and equipment or a finite-lived intangible asset). We believe that the income statement effect should be recognized prospectively in a manner similar to a change in estimate rather than in current-period income, since the recognition of the contingent consideration results from a change in facts or circumstances after the date of acquisition rather than facts that existed as of that date.

Contingent consideration that meets the definition of a derivative in ASC 815 is recognized at fair value as of the date of acquisition. The acquiring entity recognizes any changes in the carrying value of the derivative instrument after the acquisition date in accordance with ASC 815 rather than as part of the cost of the asset.

AA.2.1.2.1 Contingent Consideration When the Fair Value of the Assets Acquired Exceeds the Initial Consideration Paid

We believe that if the fair value of the assets acquired exceeds the initial consideration paid as of the date of acquisition but includes a contingent consideration arrangement, it is appropriate for an entity to analogize to the guidance in ASC 323-10-25-2A and ASC 323-10-30-2B on recognizing contingent consideration in the acquisition of an equity method investment (unless the contingent consideration arrangement meets the definition of a derivative, in which case it would be accounted for in accordance with ASC 815). That guidance states that if an entity acquires an equity method investment in which the fair value of its share of the investee’s net assets exceeds its initial cost and the agreement includes contingent consideration, the entity recognizes a liability equal to the lesser of:

• The maximum amount of contingent consideration.
• The excess of its share of the investee’s net assets over the initial cost measurement.

Like acquisitions of equity method investments, asset acquisitions are accounted for by using a cost accumulation model. Therefore, we believe that the guidance above could be applied to asset acquisitions by analogy. Accordingly, if an entity acquires a group of assets in which the fair value of the net assets exceeds its initial cost and the agreement includes contingent consideration that does not meet the definition of a derivative, the entity could recognize a liability equal to the lesser of:

• The maximum amount of contingent consideration.
• The excess of the fair value of the net assets acquired over the initial consideration paid.

2 If the assets acquired are IPR&D, see Deloitte’s Life Sciences — Accounting and Financial Reporting Update.
Accounting for Asset Acquisitions

Once recognized, the contingent consideration liability is not derecognized until the contingency is resolved and the consideration is issued or becomes issuable. In accordance with the requirements of ASC 323-10-35-14A for equity method investments, the entity recognizes “any excess of the fair value of the contingent consideration issued or issuable over the amount that was [initially] recognized as a liability . . . as an additional cost” of the asset acquisition (i.e., the amount is allocated to increase the eligible assets on a relative fair value basis). Further, “[i]f the amount initially recognized as a liability exceeds the fair value of the [contingent] consideration issued or issuable,” the entity recognizes that amount as a reduction of the cost of the asset acquisition (i.e., the amount is allocated to reduce the eligible assets on a relative fair value basis).

AA.2.2 Nonfinancial Assets (or In-Substance Nonfinancial Assets) Used as Consideration

Most asset acquisitions are effected by exchanging cash or other monetary assets for nonmonetary assets. However, in some asset acquisitions, the consideration given consists of nonfinancial assets (or in-substance nonfinancial assets) or nonmonetary assets. In that case, an entity needs to determine whether the transaction is within the scope of ASC 610-20 or ASC 845 (see Section AA.2.3). If so, the entity applies the guidance in those ASC subtopics rather than the general guidance in ASC 805-50.

Changing Lanes

In February 2017, the FASB issued ASU 2017-05, which clarifies the scope of the FASB’s guidance on nonfinancial asset derecognition in ASC 610-20 as well as the accounting for partial sales of nonfinancial assets. The ASU conforms the derecognition guidance on nonfinancial assets with the model for transactions in ASC 606, the FASB’s new revenue standard.

ASU 2017-05 also amended the “Acquisition of Assets Rather Than a Business” subsections of ASC 805-50 to clarify that “[i]f the consideration given is nonfinancial assets or in substance nonfinancial assets within the scope of Subtopic 610-20 . . ., the assets acquired shall be treated as noncash consideration and any gain or loss shall be recognized in accordance with Subtopic 610-20.” Paragraph BC39 of ASU 2017-05 states:

Stakeholders stated that they were unsure about whether to apply the guidance in [ASC] 610-20 or [ASC] 805-50 to clarify that “[i]f the consideration given is nonfinancial assets or in substance nonfinancial assets within the scope of Subtopic 610-20 . . ., the assets acquired shall be treated as noncash consideration and any gain or loss shall be recognized in accordance with Subtopic 610-20.” Paragraph BC39 of ASU 2017-05 states:

Further, ASC 610-20-15-2 indicates that “[n]onfinancial assets . . . include intangible assets, land, buildings, or materials and supplies and may have a zero carrying value.” In addition, ASC 610-20-15-5 describes an in-substance nonfinancial asset as follows:

A financial asset (for example, a receivable) promised to a counterparty in a contract if substantially all of the fair value of the assets (recognized and unrecognized) that are promised to the counterparty in the contract is concentrated in nonfinancial assets. If substantially all of the fair value of the assets that are promised to a counterparty in a contract is concentrated in nonfinancial assets, then all of the financial assets promised to the counterparty in the contract are in substance nonfinancial assets. For purposes of this evaluation, when a contract includes the transfer of ownership interests in one or more consolidated subsidiaries that is not a business, an entity shall evaluate the underlying assets in those subsidiaries.

Many of the principles in ASC 610-20 are the same as those in ASC 606 with respect to determining (1) when to derecognize a nonfinancial asset and (2) the gain or loss to recognize when a nonfinancial asset is derecognized. Specifically, ASC 610-20 incorporates the requirements for determining (1) when
a contract exists (i.e., step 1); (2) the amount of consideration to take into account in the determination of the gain or loss recognized, including an estimate of variable consideration and the application of the “constraint” (i.e., step 3); and (3) when control of the nonfinancial asset is obtained and results in the recognition of a gain or loss (i.e., step 5). In a manner similar to the accounting for a contract with a customer, an entity would apply the guidance in ASC 606-10-25-6 through 25-8 if an arrangement fails to meet the criteria in ASC 606-10-25-1 for determining the existence of a contract. In this situation, the nonfinancial asset would be (1) recognized in the statement of financial position; (2) amortized through its useful life (except for indefinite-lived intangible assets and property, plant, and equipment classified as held for sale); and (3) assessed for impairment.

ASU 2017-05 also amended ASC 610-20 to clarify that it does not apply to nonmonetary transactions within the scope of ASC 845. We believe that it may be challenging to determine whether an exchange of noncash assets is a nonmonetary exchange within the scope of ASC 845 or an exchange of nonfinancial assets within the scope of ASC 610-20 (once effective), and ASU 2017-05 provides no additional guidance on making this determination. However, we also believe that the definition of nonmonetary assets and liabilities is broader than the definitions of nonfinancial assets and in-substance nonfinancial assets.

The effective date of the amendments to ASC 805-50 is aligned with the effective date of the requirements in ASC 606. ASC 606 is effective for public companies for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2017, and for nonpublic companies for annual reporting periods beginning after December 15, 2018, and interim reporting periods within annual reporting periods beginning after December 15, 2019. If an entity decides to early adopt ASU 2017-05, it must also early adopt ASC 606 (and vice versa). See Deloitte’s A Roadmap to Applying the New Revenue Recognition Standard for more information.

AA.2.3 Nonmonetary Exchanges

If assets other than cash are given in an asset acquisition and the transaction is not within the scope of ASC 610-20 (once effective), an entity should consider whether the transaction is a nonmonetary exchange that is within the scope of ASC 845. The ASC master glossary defines “nonmonetary assets and liabilities” as “assets and liabilities other than monetary ones” and notes that examples of such assets and liabilities include “inventories; investments in common stocks; property, plant, and equipment; and liabilities for rent collected in advance.”

In a nonmonetary exchange, the acquiring entity derecognizes the assets given and recognizes (1) the nonmonetary assets acquired by using the fair value of the assets given (unless the fair value of the assets acquired is more clearly evident than the fair value of the assets surrendered) and (2) a gain or loss for the difference. However, there are three exceptions under ASC 845-10-30-3, which prohibits the use of fair value and gain or loss recognition if (1) “the fair value of neither the asset(s) received nor the asset(s) relinquished is determinable within reasonable limits,” (2) the “transaction is an exchange . . . to facilitate sales to customers,” or (3) the “transaction lacks commercial substance.” If any of these exceptions applies, the acquiring entity accounts for the transaction on the basis of the carrying amount of the nonmonetary asset given and recognizes no gain or loss (other than for impairment, if necessary).

AA.2.4 Transactions That Are Separate From an Asset Acquisition

An acquiring entity and the seller of the assets may have a preexisting relationship or other arrangement before negotiations for the acquisition begin, or they may enter into an arrangement during the negotiations that is separate from the acquisition of the assets. ASC 805-50 includes only general principles related to accounting for an asset acquisition. We believe that those principles presume that
the cost of the acquisition includes only amounts related to the acquisition of the asset or group of assets and not amounts related to separate transactions, even though the guidance does not explicitly say so. Further, we believe that in the absence of specific guidance, an entity should analogize to the guidance in ASC 805-10-25-20 and ASC 805-10-25-22, which contain guidance on identifying and accounting for transactions that are separate from a business combination. Under this guidance, the acquirer must, when applying the acquisition method, recognize “only the consideration transferred for the acquiree and the assets acquired and liabilities assumed in the exchange for the acquiree.” Any separate transactions must be accounted for separately from the business combination in accordance with the relevant GAAP.

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**Example 1**

**Asset Acquisition and Related Supply Agreement**

Company A enters into an agreement with Company B to acquire machinery and equipment that will be used to manufacture Product X. The machinery and equipment do not meet the definition of a business in ASC 805-10. In addition to stipulating a cash amount to be paid by A upon transfer of the machinery and equipment, the agreement specifies that A will provide B with a specified number of units of Product X for two years after the acquisition at a fixed per-unit price that is determined to be below market.

In determining the cost of the asset acquisition, A should take into account both the amount it paid upon transfer of the machinery and equipment and the value transferred to B under the below-market fixed-price supply agreement. Company A would recognize a balance sheet credit on the date of acquisition for the unfavorable supply contract; the credit would be recognized in income as units of Product X are delivered.

**Example 2**

**Asset Acquisition That Settles a Dispute**

Company A has an agreement with Company B that gives B the exclusive right to distribute A's goods in a specific region. Company B asserts that A has inappropriately given the distribution right to B's competitor. Company A and B decide to settle the dispute so that A reacquires the distribution right from B. The distribution right does not meet the definition of a business in ASC 805-10. Company A believes that if it does not reacquire the distribution right, it is liable to B for breach of contract.

In determining the cost of the asset acquisition, A should exclude from this cost any amount related to the dispute's settlement to avoid the capitalization of what would otherwise be an operating expense if paid separately from the asset acquisition.

In prepared remarks at the 2007 AICPA Conference on Current SEC and PCAOB Developments, Eric West, then associate chief accountant in the SEC’s Office of the Chief Accountant, discussed a fact pattern in which a company pays cash and conveys licenses to a plaintiff to settle a claim related to patent infringement and misappropriation of trade secrets. In exchange, the company receives a promise to drop the patent infringement lawsuit, a covenant not to sue with respect to the misappropriation of trade secrets claim, and a license to use the patents subject to the litigation. Mr. West notes that “[t]o properly account for this arrangement, a company must identify each item given and received and determine whether those items should be recognized.” In addition, Mr. West states the following regarding the valuation of the elements of the transaction:

> [W]e believe that it would be acceptable to value each element of the arrangement and allocate the consideration paid to each element using relative fair values. To the extent that one of the elements of the arrangement just can’t be valued, we believe that a residual approach may be a reasonable solution. In fact, we have found that many companies are not able to reliably estimate the fair value of the litigation component of any settlement and have not objected to judgments made when registrants have measured this component as a residual. In a few circumstances companies have directly measured the value of the litigation settlement component. In the fact pattern that I just described, the company may be able to calculate the value of the
settlement by applying a royalty rate to the revenues derived from the products sold using the patented technology during the infringement period. Admittedly, this approach requires judgment and we are willing to consider reasonable judgments.

Accordingly, we believe that the elements of the transaction should be valued on the basis of relative fair values unless the fair value of one of the elements cannot be estimated. In that case, a residual approach may be acceptable.

**AA.2.5 Asset Acquisitions in Which a Noncontrolling Interest Remains**

In some asset acquisitions, the acquiring entity may obtain control, but less than 100 percent of the equity interests, in a legal entity holding only an asset or group of assets such that a noncontrolling interest in the legal entity remains after the acquisition. We believe that if the legal entity is not a VIE, the acquiring entity in an asset acquisition should include the fair value of any noncontrolling interests remaining as of the date of acquisition in determining the cost to allocate to the assets or group of assets acquired by analogy to the guidance for business combinations in ASC 805-30-30-1. Under that guidance, an acquirer in a business combination must add the fair value of any noncontrolling interests remaining as of the date of acquisition to the consideration transferred to determine the amount recognized for the assets acquired and liabilities assumed. If the acquiring entity in an asset acquisition does not include the fair value of any noncontrolling interests remaining as of the date of acquisition, the asset or group of assets acquired may be recognized at an amount lower than their current fair value.

If the acquired legal entity is a VIE, entities should apply the guidance in ASC 810-10-30-4.

### Example 3

**Acquisition in Which a Noncontrolling Interest Remains**

Company A acquires an 80 percent controlling interest in a legal entity whose only asset is a finite-lived license for intellectual property. As part of the acquisition, A pays $800,000 in cash and incurs $50,000 in transaction costs for third-party advisory fees. Company A determines that the license does not meet the definition of a business in ASC 805-10 and that the entity is not a VIE. The seller of the license retains a 20 percent noncontrolling interest in the entity. The fair value of the noncontrolling interest is determined to be $195,000.

<table>
<thead>
<tr>
<th>Consideration paid</th>
<th>$ 800,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Transaction costs</td>
<td>50,000</td>
</tr>
<tr>
<td>Fair value of noncontrolling interest</td>
<td>195,000</td>
</tr>
<tr>
<td>Cost allocated to the license</td>
<td>$ 1,045,000</td>
</tr>
</tbody>
</table>

Although the fair value of the noncontrolling interest is used to measure the cost of the acquisition, A would recognize the noncontrolling interest at its proportionate share of the entity ($1,045,000 × 20 percent, or $209,000).

**AA.2.6 Asset Acquisitions in Which the Acquiring Entity Previously Held an Interest**

In some asset acquisitions, the acquiring entity may obtain control of an asset or group of assets that are held in a legal entity in which it held a noncontrolling interest immediately before the date of acquisition. ASC 805-50 provides no guidance on how an entity should account for a previously held interest in an asset acquisition when measuring the asset or group of assets acquired. In the absence of guidance, we believe that there are two alternatives if the legal entity is not a VIE. Under the first alternative, the acquiring entity in an asset acquisition would include the carrying amount of any...
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previously held interest along with the consideration paid and transaction costs incurred in determining the cost to allocate to the assets acquired. This view is consistent with the cost accumulation model because each step is measured on the basis of the respective cost incurred.

Under the second alternative, the acquiring entity in an asset acquisition would include the fair value of any previously held interest (after recognizing a gain or loss for the difference between the interest's fair value and its carrying value) along with the consideration paid and transaction costs incurred in determining the cost to allocate to the assets acquired by analogy to the guidance for business combinations in ASC 805-30-30-1. Under that guidance, an acquirer in a business combination must add the fair value of any previously held interest to the consideration transferred to determine the amount recognized for the assets acquired and liabilities assumed.

If the acquired legal entity is a VIE, entities should apply the guidance in ASC 810-10-30-4.

Example 4

**Acquisition in Which the Acquiring Entity Previously Held an Interest**

Company A has a 20 percent noncontrolling interest in a legal entity whose only asset is a finite-lived license for intellectual property. The carrying value of A's investment is $100,000, and its fair value is $200,000. Company A acquires the remaining 80 percent interest for $800,000 in cash and incurs $50,000 in transaction costs for third-party advisory fees. Company A determines that the license does not meet the definition of a business in ASC 805-10 and that the entity is not a VIE.

Under Alternative One, $950,000 would be allocated to the license as follows:

<table>
<thead>
<tr>
<th>Alternative One</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Consideration paid</td>
<td>$ 800,000</td>
</tr>
<tr>
<td>Transaction costs</td>
<td>50,000</td>
</tr>
<tr>
<td>Carrying value of previously held interest</td>
<td>100,000</td>
</tr>
<tr>
<td>Cost allocated to the license</td>
<td>$ 950,000</td>
</tr>
</tbody>
</table>

Under Alternative Two, $1,050,000 would be allocated to the license as follows:

<table>
<thead>
<tr>
<th>Alternative Two</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Carrying value of previously held interest</td>
<td>$ 100,000</td>
</tr>
<tr>
<td>Fair value of previously held interest</td>
<td>200,000</td>
</tr>
<tr>
<td>Gain recognized on remeasurement of previously held interest</td>
<td>$ 100,000</td>
</tr>
<tr>
<td>Consideration paid</td>
<td>$ 800,000</td>
</tr>
<tr>
<td>Transaction costs</td>
<td>50,000</td>
</tr>
<tr>
<td>Fair value of previously held interest</td>
<td>200,000</td>
</tr>
<tr>
<td>Cost allocated to the license</td>
<td>$ 1,050,000</td>
</tr>
</tbody>
</table>
AA.3 Allocating the Cost in an Asset Acquisition

An acquiring entity allocates the cost of an asset acquisition to the assets acquired (and liabilities assumed) on the basis of their relative fair values and is not permitted to recognize goodwill. However, if the fair values of the assets acquired and liabilities assumed are more reliably determinable, the entity measures the cost of the transaction by using these fair values. Fair value is measured in accordance with ASC 820.

Goodwill is recognized only if a business is acquired. Thus, no goodwill is recognized in an asset acquisition. Because goodwill represents the expected synergies and other benefits of combining two businesses, one would not expect goodwill to arise in an asset acquisition. If the acquiring entity's cost exceeds the fair value of the net assets acquired, the acquiring entity allocates the difference pro rata on the basis of relative fair values to increase certain of the assets acquired (see Section AA.3.1).

Bargain purchase gains are generally not recognized in an asset acquisition. If the fair value of the net assets acquired exceeds the acquiring entity's cost, the acquiring entity allocates the difference pro rata on the basis of relative fair values to reduce certain of the assets acquired (see Section AA.3.1). However, such pro rata allocation cannot reduce monetary assets below their fair values. In unusual cases, pro rata allocation either reduces the eligible assets to zero or there are no eligible assets to reduce; we do not believe that an entity should reduce monetary assets below their fair values in such circumstances. However, before recognizing a gain, the entity should consider whether (1) it has appropriately recognized all of the liabilities assumed, any contingent consideration, and any separate transactions or (2) whether the assets received are more reliably measurable than the assets given. If only monetary assets are acquired, the entity should also consider whether the transaction is, in substance, an asset acquisition. For example, if the assets being acquired are primarily cash, the transaction may be a recapitalization in substance.

AA.3.1 Exceptions to Pro Rata Allocation

Pro rata allocation of the acquiring entity's cost to the assets acquired on a relative fair value basis results in the recognition of assets at amounts that are more or less than their fair values. In deliberating ASC 805-10, ASC 805-20, and ASC 805-30, the FASB discussed a number of exceptions to the recognition and fair value measurement principles in a business combination for assets or liabilities for which the subsequent accounting is prescribed by other GAAP and application of such GAAP would result in the acquirer's recognition of an immediate gain or loss. Examples of such exceptions include assets held for sale, employee benefits, and income taxes. ASC 805-50 provides only general guidance on allocating cost in an asset acquisition. However, we believe that the same principles should apply to an asset acquisition. That is, an acquiring entity should not recognize an asset at an amount that would
result in the entity’s recognition of an immediate gain or loss as a result of the subsequent application of GAAP if no economic gain or loss has occurred (with the exception of IPR&D assets with no alternative future use, which are discussed in Section AA.3.4.2).

Therefore, we believe that certain assets should be recognized at the amounts required by applicable U.S. GAAP or should not be recognized at amounts that exceed their fair values. Such assets (and liabilities) include:

- Cash and other financial assets (other than investments accounted for under the equity method).
- Other current assets.
- Assets subject to fair value impairment testing, such as indefinite-lived intangible assets.
- Assets held for sale.
- Income taxes.
- Employee benefits.
- Indemnification assets (see Section AA.3.3).

### Example 5

#### Excess of Cost Over the Fair Values of the Assets Acquired

Company A acquires three assets from Company B: machinery and equipment with a fair value of $20,000, a building with a fair value of $50,000, and an indefinite-lived intangible asset with a fair value of $30,000. The total cost of the acquisition, including transaction costs, is $120,000. Company A has determined that the assets do not constitute a business and allocates the cost as follows:

<table>
<thead>
<tr>
<th>Fair Value (ASC 820)</th>
<th>Percentage of Fair Value*</th>
<th>Cost of the Acquisition Less Ineligible Asset</th>
<th>Allocated Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Machinery and equipment</td>
<td>$20,000</td>
<td>$90,000</td>
<td>$25,714</td>
</tr>
<tr>
<td>Building</td>
<td>50,000</td>
<td>71</td>
<td>64,286</td>
</tr>
<tr>
<td>Indefinite-lived intangible asset</td>
<td>$30,000</td>
<td>30,000</td>
<td></td>
</tr>
</tbody>
</table>

*Because the indefinite-lived intangible asset is not recognized at an amount that exceeds its fair value, the percentages are calculated on the basis of only the eligible assets ($20,000 ÷ $70,000 and $50,000 ÷ $70,000).

Sometimes the fair value of the net assets acquired exceeds the acquiring entity’s cost (i.e., a bargain purchase), though this is unusual. Allocation of a bargain purchase will reduce assets below their fair values. We believe there are two acceptable views on how to allocate the acquiring entity’s cost in such cases. Under the first alternative, the same assets that are ineligible for pro rata allocation when cost exceeds the fair value of the assets should also be ineligible for pro rata allocation in a bargain purchase.
Example 6

**Excess of Fair Values of the Assets Acquired Over Cost (Alternative One)**

Assume the same facts as in Example 5, except that the total cost of the acquisition, including transaction costs, is $90,000. Company A’s cost is allocated as follows:

<table>
<thead>
<tr>
<th>Fair Value (ASC 820)</th>
<th>Percentage of Fair Value*</th>
<th>Cost of the Acquisition Less Ineligible Asset</th>
<th>Allocated Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Machinery and equipment</td>
<td>$ 20,000</td>
<td>29</td>
<td>$ 60,000</td>
</tr>
<tr>
<td>Building</td>
<td>50,000</td>
<td>71</td>
<td>$ 60,000</td>
</tr>
<tr>
<td>Indefinite-lived intangible asset</td>
<td>30,000</td>
<td></td>
<td>30,000</td>
</tr>
<tr>
<td>$ 100,000</td>
<td></td>
<td></td>
<td>$ 90,000</td>
</tr>
</tbody>
</table>

* Because the indefinite-lived intangible asset is recognized at its fair value, the percentages are calculated on the basis of only the eligible assets ($20,000 ÷ $70,000 and $50,000 ÷ $70,000).

Under the second alternative, it is appropriate to allocate a bargain purchase to any asset for which the subsequent application of U.S. GAAP would not result in an immediate gain, such as indefinite-lived intangible assets or assets held for sale.

Example 7

**Excess of Fair Values of the Assets Acquired Over Cost (Alternative Two)**

Assume the same facts as in Example 5, except that the total cost of the acquisition, including transaction costs, is $90,000. Company A’s cost is allocated as follows:

<table>
<thead>
<tr>
<th>Fair Value (ASC 820)</th>
<th>Percentage of Fair Value*</th>
<th>Cost of the Acquisition Less Ineligible Asset</th>
<th>Allocated Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Machinery and equipment</td>
<td>$ 20,000</td>
<td>20</td>
<td>$ 90,000</td>
</tr>
<tr>
<td>Building</td>
<td>50,000</td>
<td>50</td>
<td>$ 90,000</td>
</tr>
<tr>
<td>Indefinite-lived intangible asset</td>
<td>30,000</td>
<td>30</td>
<td>$ 90,000</td>
</tr>
<tr>
<td>$ 100,000</td>
<td></td>
<td></td>
<td>$ 90,000</td>
</tr>
</tbody>
</table>

* This example assumes that an indefinite-lived intangible asset can be recognized at less than its fair value (but not at greater than its fair value), so the total cost must be allocated to all of the acquired assets.

AA.3.2 Contingencies

An entity accounts for contingencies acquired or assumed in an asset acquisition in accordance with ASC 450. Loss contingencies are recognized when it is probable that they will occur and they can be reasonably estimated. Gain contingencies are not recognized until they are realized and therefore are not recognizable in an asset acquisition. If an acquiring entity acquires a gain or loss contingency in an asset acquisition but the contingency does not qualify for recognition on the date of acquisition, the
entity would allocate the cost to the acquired assets and may initially recognize certain assets at more or less than their fair values because of the nonrecognition of the contingency.

**AA.3.3 Indemnification Assets**

The seller in an asset acquisition may contractually indemnify the acquiring entity for the outcome of a contingency or uncertainty related to all or part of a specific asset or liability. For example, the seller may indemnify the acquiring entity against losses above a specified amount on a liability that arises from a particular contingency; in other words, the seller will guarantee that the acquiring entity’s liability will not exceed a specified amount. As a result, the acquiring entity obtains an indemnification asset.

Under ASC 805-20-25-27, an acquirer in a business combination must “recognize an indemnification asset at the same time that it recognizes the indemnified item, measured on the same basis as the indemnified item, subject to the need for a valuation allowance for uncollectible amounts.” We believe that an entity should also apply this guidance by analogy in an asset acquisition.

**AA.3.4 Intangible Assets**

An entity recognizes intangible assets that are acquired in an asset acquisition if they meet the asset recognition criteria in FASB Concepts Statement 5, even if they are not separable or do not arise from contractual rights. There is a lower threshold for recognizing intangible assets in an asset acquisition than in a business combination (with the exception of IPR&D, which is discussed in Section AA.3.4.2). In a business combination, if the consideration transferred includes amounts for intangible assets that do not qualify for recognition (e.g., assembled workforce), those unrecognized intangible assets are subsumed into goodwill but the assets acquired are still generally recognized at their fair values. However, in an asset acquisition, no goodwill is recognized. If the consideration paid includes amounts for intangible assets that were not separately recognized, the cost of the acquisition would be allocated to the recognizable assets and those assets may be recognized at amounts that exceed their fair values. Since there is no residual into which unrecognized intangible assets could be subsumed, the FASB decided that the threshold for recognizing intangible assets in an asset acquisition should be lower than in a business combination.

**AA.3.4.1 Assembled Workforce**

ASC 805-20-55-6 defines an assembled workforce as “an existing collection of employees that permits the acquirer to continue to operate an acquired business from the acquisition date.” Under ASC 805-20-55-6, an assembled workforce is not recognized in a business combination because it neither is separable nor arises from contractual rights (i.e., identifiable). However, in an asset acquisition, an assembled workforce would generally meet the asset recognition criteria in FASB Concepts Statement 5 and would be separately recognized. But because an assembled workforce is often associated with substantive processes, the presence of an assembled workforce may indicate that the acquisition involves a business rather than an asset or a group of assets. An entity must evaluate all facts and circumstances in determining whether a group of acquired assets constitutes a business under ASC 805.

**AA.3.4.2 In-Process Research and Development**

An acquiring entity must allocate, on the basis of relative fair values, the cost of the acquisition to both the tangible and intangible research and development assets acquired. On the date of acquisition, the acquiring entity expenses IPR&D assets with no alternative future use and capitalizes those with an alternative future use in accordance with ASC 730.
One of the most significant differences between the accounting for an asset acquisition and that for a business combination lies in the accounting for IPR&D assets. In a business combination, the acquirer must recognize all IPR&D assets at fair value and initially characterize them as indefinite-lived intangible assets, regardless of whether the IPR&D assets have an alternative future use. In EITF Issue 09-2, the Task Force considered amending ASC 730 with respect to IPR&D assets acquired in an asset acquisition; however, the Task Force was unable to reach a consensus and removed the project from its agenda. Therefore, entities continue to apply the guidance in ASC 730 in accounting for IPR&D assets acquired in an asset acquisition.

**AA.3.4.3 Defensive Intangible Assets**

ASC 805-20-30-6 states that “[t]o protect its competitive position, or for other reasons, the acquirer may intend not to use an acquired nonfinancial asset actively, or it may not intend to use the asset according to its highest and best use.” While such assets are not being actively used, they are most likely contributing to an increase in the value of other assets owned by the acquiring entity. Common examples of such assets, which are known as “defensive assets,” include brand names and patents.

While ASC 805-50 does not address the accounting for defensive intangible assets, we believe that because such assets must be recognized under ASC 805-20, they meet the asset recognition criteria in FASB Concepts Statement 5 and therefore should be recognized in an asset acquisition on the basis of their relative fair values. Fair value would be measured in accordance with ASC 820-10, and the asset’s highest and best use by market participants would be assumed, both initially and for subsequent impairment testing.

**AA.3.5 Deferred Taxes**

ASC 740-10-25-49 through 25-55 provide guidance on accounting for acquired temporary differences in certain purchase transactions that are not accounted for as business combinations (i.e., asset acquisitions). Because goodwill is not recognized in an asset acquisition, an entity generally recognizes deferred taxes for temporary book/tax differences in an asset acquisition by using the simultaneous equations method.

For more information about accounting for income taxes in an asset acquisition, see Deloitte's *A Roadmap to Accounting for Income Taxes*.

**AA.3.6 Lease Classification**

In a business combination, an acquiree does not reconsider the classification of its leases in accordance with ASC 805-20-25-8(a) unless the lease agreement is modified as part of the acquisition. Therefore, the acquiree's classification of its lease agreements generally carries over to the acquirer. ASC 805-50 does not address classification of leases acquired in an asset acquisition. In the absence of guidance, some believe that it is appropriate to analogize to the business combination guidance. However, we believe that acquiring leases in an asset acquisition in which the acquiring entity becomes the lessee is similar to a transaction in which an entity subleases an asset. Under ASC 840-10-25-32, when an entity enters into an agreement to sublease an asset, the sublessee must classify the lease as capital or operating in accordance with the criteria in ASC 840-10-25-1. Similarly, we believe that the acquiring entity should reassess the classification of lease contracts in which it becomes the lessee as of the date of acquisition.

If the acquiring entity becomes the lessor in an acquired lease arrangement, the guidance in ASC 350-30 applies. The cost of the acquisition is allocated to tangible assets (e.g., land and buildings) and any in-place lease intangible asset on the basis of their relative fair values. The fair value of assets does not
incorporate any value from the leases. For example, the fair value of the land and building is measured as if the building was vacant.

**AA.3.7 Asset Acquisition in Which the Acquiring Entity Retains Control of an Asset Used as Consideration**

In some asset acquisitions, the consideration given may include assets or liabilities that remain within the combined entity after the acquisition. Therefore, the acquiring entity controls them before and after the asset acquisition. Under ASC 805-30-30-8, in a business combination, the acquirer must recognize those assets and liabilities at their carrying amounts immediately before the acquisition date; the acquirer is precluded from recognizing a gain or loss on assets or liabilities it controls both before and after the business combination. While ASC 805-50 does not address this issue, we believe that it is appropriate to apply the guidance in ASC 805-30-30-8 to asset acquisitions by analogy.

**Example 8**

**Assets Transferred as Consideration That Remain Under the Control of the Acquiring Entity**

Company A enters into an agreement to acquire an 80 percent interest in Entity B for $875,000 in cash and equipment; A incurs $50,000 in transaction costs for third-party advisory fees. Entity B's only assets include three buildings, which do not meet the definition of a business in ASC 805-10. The equipment A gives as consideration will be transferred not to the seller but to B and will therefore remain in the combined entity. This equipment has a carrying value of $500,000 and a fair value of $625,000. The three buildings A acquires have fair values of $300,000, $500,000, and $450,000, a total of $1,250,000.

<table>
<thead>
<tr>
<th>Description</th>
<th>Initial Measurement</th>
<th>Percentage of Fair Value**</th>
<th>Amount Allocated to Acquired Buildings</th>
<th>Allocated Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash paid</td>
<td>$ 875,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transaction costs</td>
<td>50,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Carrying value of the equipment transferred to B</td>
<td>500,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fair value of noncontrolling interest</td>
<td>375,000*</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>1,800,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: carrying value of the equipment transferred to B</td>
<td>(500,000)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Amount allocable to acquired buildings</td>
<td>$ 1,300,000</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* Calculated as 20 percent of the sum of $1,250,000 and the fair value of the equipment of $625,000.

** Because the equipment transferred by A must be recognized at its carrying amount, the percentages are calculated on the basis of only the fair value of the acquired assets ($300,000, $500,000, $450,000, and $625,000).
AA.3.8 Measurement Period

In a business combination, an acquirer is allowed a period during which it may adjust provisional amounts recognized as of the acquisition date. This time frame is referred to as the measurement period. ASC 805-50 does not address the concept of a measurement period and, in practice, entities have not been provided a measurement period in an asset acquisition. We believe that because asset acquisitions are generally less complex than business combinations, the acquiring entity should be able to obtain any valuations and information necessary to complete its accounting for an asset acquisition before its next reporting date.

AA.3.9 Subsequent Accounting for Assets Acquired or Liabilities Assumed in an Asset Acquisition

The initial measurement of an asset acquired or liability assumed in an asset acquisition does not affect its subsequent accounting. The subsequent accounting for contingent consideration is described in Section AA.2.1.2. Otherwise, the acquirer subsequently accounts for the assets or any liabilities assumed or incurred in accordance with the appropriate GAAP, as applicable.

AA.4 Disclosures

ASC 805-50 does not prescribe any disclosure requirements for asset acquisitions. However, the acquiring entity will need to provide disclosures in accordance with other GAAP depending on the assets acquired or the liabilities assumed or incurred. For example:

- ASC 360-10-50-1 requires disclosure of the balances of major classes of depreciable assets, by nature or function, and accumulated depreciation on the balance sheet date; depreciation expense for the period; and a general description of the method or methods used to compute depreciation with respect to major classes of depreciable assets.
- ASC 350-30-50-1 includes disclosure requirements for intangible assets acquired either individually or as part of a group of assets.
- ASC 450-20-50 requires disclosures regarding loss contingencies.
- ASC 845-10-50-1 includes specific disclosure requirements for nonmonetary transactions.

In addition, depending on the size of the asset acquisition, acquiring entities may decide to provide some of the disclosures prescribed in ASC 805-10-50, ASC 805-20-50, or ASC 805-30-50 for a business combination. For example, disclosures about the reason for the acquisition, the amounts recognized as of the date of acquisition for each major class of assets acquired and liabilities assumed, and information about any separate transactions may enhance users' understanding of the transaction.

AA.5 SEC Reporting Considerations Related to Asset Acquisitions

When an SEC registrant acquires an asset or a group of assets, the registrant may be required to report the acquisition on Form 8-K, Item 2.01. The nature of the registrant's disclosures depends on whether the asset or group of assets (1) represents a business for SEC reporting purposes or (2) is significant.
The definition of a business in SEC Regulation S-X, Rule 11-01(d), for SEC reporting purposes differs from the definition of a business in ASC 805-10 for U.S. GAAP accounting purposes. Accordingly, the registrant must perform a separate evaluation under SEC Regulation S-X, Rule 11-01(d), to determine its SEC reporting requirements. In addition, the significance tests for an asset or a group of assets that represents a business for SEC reporting differ from the significance tests for an asset or a group of assets that does not represent a business. In certain circumstances, a registrant may be required to file separate pre-acquisition historical financial statements for the acquired asset or group of assets under SEC Regulation S-X, Rule 3-05, as well as pro forma financial information that gives effect to the acquisition under SEC Regulation S-X, Article 11.

**Connecting the Dots**

The sections below provide general guidance on, and assume that registrants have a general understanding of, the reporting requirements in SEC Regulation S-X, Rule 3-05, (under which separate pre-acquisition historical financial statements of the acquired business must be filed when the acquisition of a significant business has occurred or is probable), and SEC Regulation S-X, Article 11 (which establishes the requirements for pro forma financial information). Registrants should also consider the guidance in Topics 2 and 3 of the SEC Division of Corporation Finance Financial Reporting Manual and may consult with their legal advisers and independent accountants regarding these requirements.

**AA.5.1 Form 8-K Reporting Obligations**

A registrant is required to periodically file current reports on Form 8-K to inform investors of certain events. Under Form 8-K, Item 2.01, the registrant must file a Form 8-K in four business days after consummation of an acquisition of (1) a significant amount of assets or (2) a business that is significant. A registrant’s filing requirements vary on the basis of whether the acquired asset or group of assets (1) represents a business for SEC reporting purposes and (2) is significant. See Section AA.5.2 below for a discussion of the definition of a business for SEC reporting purposes.

Instruction 4 of Item 2.01, Form 8-K, discusses significance and states:

An acquisition or disposition shall be deemed to involve a significant amount of assets:

(i) if the registrant’s and its other subsidiaries’ equity in the net book value of such assets or the amount paid or received for the assets upon such acquisition or disposition exceeded 10% of the total assets of the registrant and its consolidated subsidiaries; or

(ii) if it involved a business (see 17 CFR 210.11-01(d)) that is significant (see 17 CFR 210.11-01(b)).

See Section AA.5.3 and Section AA.5.4, respectively, below for a discussion of the Form 8-K reporting requirements under Item 2.01 for the acquisition of an asset or group of assets that (1) does not meet the definition of a business for SEC reporting purposes and (2) meets the definition of a business for SEC reporting purposes.

**Connecting the Dots**

Item 1.01 of Form 8-K may also require a registrant to file a Form 8-K when it has entered into a material definitive agreement for an acquisition (e.g., when it executes a contract for an acquisition). Item 1.01 of Form 8-K is generally filed earlier than Item 2.01 of Form 8-K, which the registrant is not required to file until the acquisition is consummated.
AA.5.2 Definition of a Business for SEC Reporting Purposes

The definition of a business for SEC reporting purposes in Regulation S-X, Rule 11-01(d), differs from the definition in ASC 805-10 for U.S. GAAP accounting purposes. A registrant must carefully evaluate the requirements in SEC Regulation S-X, Rule 11-01(d), to determine whether the asset or group of assets acquired represents a business for SEC reporting purposes. As noted in paragraph 2010.1 of the SEC Financial Reporting Manual, it is possible for the determination under SEC Regulation S-X, Rule 11-01(d), to differ from that under ASC 805-10. Therefore, it is possible for an acquired asset or group of assets to meet the definition of a business in ASC 805-10 and be accounted for as a business combination but not to meet the definition of a business in SEC Regulation S-X, Rule 11-01(d), and be reported for as an asset acquisition, or vice versa.

The definition of a business in SEC Regulation S-X, Rule 11-01(d), states, in part:

[T]he term business should be evaluated in light of the facts and circumstances involved and whether there is sufficient continuity of the acquired entity's operations prior to and after the transactions so that disclosure of prior financial information is material to an understanding of future operations. A presumption exists that a separate entity, a subsidiary, or a division is a business.

However, a lesser component (e.g., a product line) may also constitute a business. SEC Regulation S-X, Rule 11-01(d), lists several factors an entity should consider in determining whether such a component constitutes a business. These factors include:

- Whether the nature of the revenue-producing activity will generally remain the same after the acquisition.
- Whether any of the following will remain after the acquisition: the physical facilities, employee base, market distribution system, sales force, customer base, operating rights, production techniques, or trade names.

The SEC staff's analysis of whether an acquisition meets the definition of a business focuses primarily on whether the nature of the revenue-producing activity generally remains the same after the acquisition. In addition, the note to paragraph 2010.2 of the SEC Financial Reporting Manual states, in part:

New carrying values of assets, or changes in financing, management, operating procedures, or other aspects of the business are not unusual following a business acquisition. Such changes typically do not eliminate the relevance of historical financial statements.

If the revenue-producing activity continues after the acquisition, it is presumed that a business was acquired and that prior financial information would be relevant to the understanding of future operations.

The form in which the transaction takes place typically will not affect the determination of whether the acquisition is a business. For example, the transaction may involve the acquisition of the stock of an entity or the acquisition of selected assets and the assumption of selected liabilities of that entity. Either form can constitute the acquisition of a business.
Example 9

Acquisition Does Not Meet the Definition of a Business for SEC Reporting Purposes

This example summarizes an issue addressed at the March 2001 CAQ SEC Regulations Committee joint meeting with the SEC staff (the “joint meeting”).

Registrant A acquired a power plant from Company X. Before the acquisition, the output from the power plant was historically transferred to X's transmission and distribution operations. During some periods, X sold a small amount of the power plant output to third parties. Registrant A expected to sell the output from the power plant to third parties, including X. At issue is whether A’s acquisition of the power plant meets the definition of a business under SEC Regulation S-X, Rule 11-01(d).

According to the SEC staff, the acquisition of the power plant does not meet the definition of a business for SEC reporting purposes. At the joint meeting, the SEC staff noted:

- Generally, the absence of third party sales is a persuasive indicator that historical information would not be meaningful. However, determinable market prices directly attributable to a commodity (such as posted oil prices for a producing property) may permit the preparation of meaningful historical financial information.

The SEC staff also stated that “pre-clearance may continue to be wise in many circumstances.”

Example 10

Acquisition Does Meet the Definition of a Business for SEC Reporting Purposes

This example summarizes an issue discussed with the SEC staff.

Registrant B acquired 100 contracts, intellectual property, leases, and certain other assets from Registrant C. Registrant B also acquired the right and obligation to hire approximately 1,200 employees from C. Upon completion of the acquisition, B performed the activities obligated by the contracts; however, there were some changes in the cost structure and management. At issue is whether the acquisition meets the definition of a business under SEC Regulation S-X, Rule 11-01(d).

The SEC staff concluded that B’s acquisition of 100 contracts, intellectual property, leases, and certain other assets meets the definition of a business under SEC Regulation S-X, Rule 11-01(d). The SEC staff noted that the contractual nature of the revenue streams acquired suggests that the revenue-producing activity will generally remain the same. Changes in cost structure and management are not unusual after an acquisition. The SEC staff believes that the historical financial statements would be relevant to the understanding of future operations.

Paragraphs 2010.3 through 2010.6 of the SEC Financial Reporting Manual note that the following types of acquisitions may also meet the definition of a business:

- An investment accounted for under the equity method — According to SEC Regulation S-X, Rule 3-05(a)(1)(i), the definition of a business acquisition includes the purchase of an interest in a business accounted for under the equity method. This definition also includes the acquisition of a joint venture investment that is accounted for under the equity method.

- A working interest in an oil and gas property — As discussed in paragraph 2010.4 of the SEC Financial Reporting Manual, the Office of the Chief Accountant of the Division of Corporation Finance (1) “considers the acquisition of a working interest in an oil and gas property to be a business for reporting purposes” and (2) refers registrants to paragraph 2065.11 of the SEC Financial Reporting Manual for guidance on when abbreviated financial statements will be accepted.

- Customer deposits at bank branches — Paragraph 2010.5 of the SEC Financial Reporting Manual states that the “assumption of customer deposits at bank branches may constitute the acquisition of a business if historical revenue producing activity is reasonably traceable to
the management or customer and deposit base of the acquired branches, and that activity will remain generally the same following the acquisition."

- **Blocks of insurance policies acquired by an insurance company and liabilities assumed in reinsurance transactions** — Paragraph 2010.6 of the SEC Financial Reporting Manual states that “[a]quisitions of blocks of insurance policies by an insurance company or the assumption of policy liabilities in reinsurance transactions may also be deemed the acquisition of a business because the right to receive future premiums generally indicates continuity of historical revenues. The degree of continuity between historical investment income streams and the assets acquired to fund the acquired policy liabilities should also be considered.”

In addition, a cost center (i.e., part of a company that incurs internal expenses but does not generate revenues) or an entity that has not commenced planned principal operations, or has commenced planned principal operations but has not generated significant revenue, may also meet the definition of a business. In such circumstances, the criteria in SEC Regulation S-X, Rule 11-01(d), should be evaluated.

AA.5.3 **Form 8-K Reporting — Acquisition of Assets That Does Not Meet the Definition of a Business for SEC Reporting Purposes**

If the acquired asset or group of assets does not meet the definition of a business for SEC reporting purposes, the acquisition should be regarded as an asset acquisition and reported under Form 8-K, Item 2.01, if it exceeds the 10 percent threshold specified in the two significance tests set forth in Instruction 4. These tests are similar to the asset and investment tests in SEC Regulation S-X, Rule 1-02(w).

The required disclosures for acquisitions of significant assets differ from the disclosures required for a significant business acquisition. Since SEC Regulation S-X, Rule 3-05, does not apply, no historical financial statements need to be filed. However, the disclosures in Item 2.01 of Form 8-K should clearly (1) describe the assets acquired, (2) describe the anticipated effects on the registrant’s financial condition, and (3) indicate that the acquisition did not constitute the acquisition of a business. When such information would be material to investors, the registrant may consider including limited pro forma balance sheet information reflecting the effects of the asset acquisition (or include a narrative discussion, for example, when adjustments are easily understood).

The initial Form 8-K must be filed four business days after consummation of the acquisition. If material, the pro forma balance sheet information must be included in the initial Form 8-K. The 71-calendar-day extension in Form 8-K, Item 9.01, that is available for a business acquisition is not available for an asset acquisition.

AA.5.4 **Form 8-K Reporting — Acquisition of Assets That Meets the Definition of a Business for SEC Reporting Purposes**

If the acquired asset or group of assets meets the definition of a business for SEC reporting purposes, the registrant should use Item 2.01 of Form 8-K to report the acquisition if it is significant. As noted in Instruction 4, a business is significant if any of the results of the three significance tests in SEC Regulation S-X, Rule 1-02(w) (i.e., the asset, income, and investment tests), exceed 20 percent.

To comply with Form 8-K, Item 2.01, the registrant must apply SEC Regulation S-X, Rule 3-05, which generally requires the filing of separate pre-acquisition historical audited financial statements for the acquired business. The financial statement periods that a registrant is required to file (i.e., one, two, or three years of audited financial statements) will be based on the significance level determined after performance of any of the three tests in SEC Regulation S-X, Rule 1-02(w). Unaudited financial statements as of and for the appropriate interim periods preceding the acquisition may also be
required. In addition, the registrant must provide pro forma financial information in accordance with SEC Regulation S-X, Article 11, to give effect to the acquisition (see Section AA.5.6 below).

The initial Form 8-K must be filed within four business days after consummation of the acquisition. If available, the historical and pro forma financial statements may be filed along with the initial Form 8-K. Otherwise, the registrant has an additional 71 calendar days to file an amended Form 8-K that includes these historical and pro forma financial statements.

**Connecting the Dots**

A Form 8-K is not the only type of SEC filing in which financial statements of a significant consummated business acquisition may be required. For example, such information may also be required in a registration statement, prospectus supplement, or proxy statement.

A registrant is not required to file a Form 8-K that includes financial statements for a significant probable business acquisition. However, such information may be required in connection with a registration statement, prospectus supplement, or proxy statement.

**AA.5.5 Form and Content of Financial Statements for an Asset or a Group of Assets That Meets the Definition of a Business for SEC Reporting Purposes**

The form and content of the historical financial statements of an asset or group of assets that meets the definition of a business for SEC reporting purposes may be as follows:

**Full Financial Statements**

If the acquired asset or group of assets represents substantially all of an entity, the entire entity’s full audited financial statements are generally required. Paragraph 2065.1 of the SEC Financial Reporting Manual states that in these circumstances, “full audited financial statements of the entity are presumed to be necessary in order to provide investors with the complete and comprehensive financial history of the acquired business.”

**Carve-Out Financial Statements**

Paragraph 2065.2 of the SEC Financial Reporting Manual notes that if the acquired asset or group of assets does not represent substantially all of the selling entity, “financial statements of the larger entity of which the acquired business was a part may not be informative.” Therefore, the audited financial statements should only represent the selected parts of the entity acquired, excluding the operations retained by the seller. These financial statements are often referred to as **carve-out financial statements**. Carve-out financial statements include a balance sheet, a statement of operations (through net income), a statement of cash flows, a stockholders’ equity statement, and the respective notes to the financial statements. The SEC staff believes that carve-out financial statements should reflect (1) all assets and liabilities of the acquired business even if they are not acquired or assumed as part of the acquisition and (2) all costs of doing business. For further discussion, see Deloitte’s forthcoming *A Roadmap to Accounting and Financial Reporting for Carve-Out Transactions*. Also see SEC SAB Topic 1.B as well as Sections 7200 and 7400 of the SEC Financial Reporting Manual.

**Abbreviated Financial Statements**

In certain circumstances, carve-out financial statements may not be practicable to prepare, such as when the acquired asset or group of assets is a small portion or a product line of a much larger business and is not a stand-alone entity; distinct and separate accounts necessary to present the full financial statements of the business were not maintained; and separate audited financial statements have never
been prepared. In such instances, the SEC staff may allow registrants to provide abbreviated financial information — that is, audited statements of assets acquired and liabilities assumed (in lieu of a full balance sheet) and audited statements of revenues and direct expenses (in lieu of a full statement of operations) — to meet the financial statement requirements in SEC Regulation S-X, Rule 3-05.

Except for acquisitions of certain oil and gas properties (discussed in paragraph 2065.11 of the SEC Financial Reporting Manual), the use of this abbreviated financial information in lieu of carve-out financial statements is not permitted without prior written request to the Office of the Chief Accountant of the Division of Corporation Finance.

For additional information about carve-out financial statements, including abbreviated financial statements, see Section 2065 of the SEC Financial Reporting Manual.

**Connecting the Dots**

When a registrant acquires (or it is probable that it will acquire) real estate operations, the registrant may be required to provide abbreviated income statements in accordance with SEC Regulation S-X, Rule 3-14, which differ in certain respects from those provided under SEC Regulation S-X, Rule 3-05. For additional information about real estate operations, see Section 2300 of the SEC Financial Reporting Manual.

**AA.5.6 Pro Forma Financial Information**

SEC Regulation S-X, Article 11, lists several circumstances in which a registrant may be required to provide pro forma financial information, including when an acquisition of a significant business has occurred or is probable. Such circumstances include those in which the acquired asset or group of assets meets the definition of a business for SEC reporting purposes. Pro forma financial information for the appropriate periods may be required in a registration statement, proxy statement, or Form 8-K. For additional SEC interpretive guidance on SEC Regulation S-X, Article 11, see Topic 3 of the SEC Financial Reporting Manual.

When a registrant acquires an asset or a group of assets that does not meet the definition of a business for SEC reporting purpose, it may consider including limited pro forma balance sheet information (or a narrative discussion, for example, in cases in which adjustments are easily understood) reflecting the effects of the asset acquisition when such information would be material to investors.
Appendix A — Selected Glossary Terms From ASC 805-50

<table>
<thead>
<tr>
<th><strong>ASC 805-50-20</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Acquisition Date (or Date of Acquisition)</strong></td>
</tr>
<tr>
<td>The date on which the acquirer obtains control of the acquiree.</td>
</tr>
</tbody>
</table>

**Business**

An integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing a return in the form of dividends, lower costs, or other economic benefits directly to investors or other owners, members, or participants. Additional guidance on what a business consists of is presented in paragraphs 805-10-55-4 through 55-9.

**Note:** The following definition is Pending Content; see Transition Guidance in paragraph 805-10-65-4.

Paragraphs 805-10-55-3A through 55-6 and 805-10-55-8 through 55-9 define what is considered a business.

**Business Combination**

A transaction or other event in which an acquirer obtains control of one or more businesses. Transactions sometimes referred to as true mergers or mergers of equals also are business combinations.

**Interests**

Used broadly to mean ownership interests of investor-owned entities; owner, member, or participant interests of mutual entities; and owner or member interests in the net assets of not-for-profit entities.

**Fair Value**

The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

**Goodwill**

An asset representing the future economic benefits arising from other assets acquired in a business combination or an acquisition by a not-for-profit entity that are not individually identified and separately recognized. For ease of reference, this term also includes the immediate charge recognized by not-for-profit entities in accordance with paragraph 958-805-25-29.
Appendix B — Glossary of Standards and Other Literature

The following are the titles of standards and other literature mentioned in this publication:

**FASB Accounting Standards Codification (ASC) Topics**
- ASC 323, Investments — Equity Method and Joint Ventures
- ASC 350, Intangibles — Goodwill and Other
- ASC 360, Property, Plant, and Equipment
- ASC 450, Contingencies
- ASC 606, Revenue From Contracts With Customers
- ASC 610, Other Income
- ASC 715, Compensation — Retirement Benefits
- ASC 730, Research and Development
- ASC 740, Income Taxes
- ASC 805, Business Combinations
- ASC 810, Consolidation
- ASC 815, Derivatives and Hedging
- ASC 820, Fair Value Measurement
- ASC 835, Interest
- ASC 840, Leases
- ASC 845, Nonmonetary Transactions
- ASC 958, Not-for-Profit Entities

**FASB Accounting Standards Updates (ASUs)**
- ASU 2017-05, Other Income — Gains and Losses From the Derecognition of Nonfinancial Assets (Subtopic 610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets
- ASU 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business
FASB Concepts Statement (Pre-Codification Literature)
Concepts Statement 5, Recognition and Measurement in Financial Statements of Business Enterprises

EITF Issue (Pre-Codification Literature)
Issue 09-2, “Research and Development Assets Acquired in an Asset Acquisition”

SEC Division of Corporation Finance Financial Reporting Manual
Topic 2, “Other Financial Statements Required”
Topic 3, “Pro Forma Financial Information”
Topic 7, “Related Party Matters”

Rule 1-02, “Definitions of Terms Used in Regulation S-X”
Rule 3-05, “Financial Statements of Businesses Acquired or to Be Acquired”
Rule 3-14, “Special Instructions for Real Estate Operations to Be Acquired”
Article 11, “Pro Forma Financial Information”
Rule 11-01, “Presentation Requirements”

SEC Staff Accounting Bulletin (SAB) Topic
SAB Topic 5.A, “Expenses of Offering”
### Appendix C — Abbreviations

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
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<tbody>
<tr>
<td>AICPA</td>
<td>American Institute of Certified Public Accountants</td>
</tr>
<tr>
<td>ASC</td>
<td>FASB Accounting Standards Codification</td>
</tr>
<tr>
<td>ASU</td>
<td>FASB Accounting Standards Update</td>
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<td>EITF</td>
<td>Emerging Issues Task Force</td>
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<td>FASB</td>
<td>Financial Accounting Standards Board</td>
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<td>GAAP</td>
<td>generally accepted accounting principles</td>
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<td>IPR&amp;D</td>
<td>in-process research and development</td>
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<td>PCAOB</td>
<td>Public Company Accounting Oversight Board</td>
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<td>SAB</td>
<td>SEC Staff Accounting Bulletin</td>
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<td>SEC</td>
<td>Securities and Exchange Commission</td>
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<td>VIE</td>
<td>variable interest entity</td>
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