



Anquillare, Ruocco, Traester and Company
Certified Public Accountants and Consultants
98 Elm Street, P.O. Box 308, West Haven, CT 06516
203-932-2931/ Fax: 203-932-9962
www.artcpas.com

FASB Issues New Guidance on Nonprofit Mergers and Acquisitions July 2009

The Financial Accounting Standards Board (FASB) recently issued Statement Number 164 to provide guidance on the accounting associated with a combination of a nonprofit entity with one or more other nonprofit entities, businesses, or nonprofit activities. The statement establishes principles and requirements on how a nonprofit entity:

- Determines whether a combination is a merger or an acquisition
- Applies the carryover method in accounting for a merger
- Applies the acquisition method in accounting for an acquisition
- Determines what information to disclose in financial statements.

Statement Number 164 is effective for:

- Mergers for which the merger date is on or after the beginning of an *initial* reporting period beginning on or after December 15, 2009
- Acquisitions for which the acquisition date is on or after the beginning of the first *annual* reporting period beginning on or after December 15, 2009.

Statement Number 164 may NOT be applied to mergers or acquisitions before those dates, according to the FASB guidance.

The Statement does not apply to:

- The formation of a joint venture
- The acquisition of an asset or a group of assets that does not constitute either a business or a nonprofit activity
- A combination between not-for-profit entities, businesses, or nonprofit activities under common control
- A transaction or other event in which a not-for-profit entity obtains control of another entity but does not consolidate that entity, as permitted or required by AICPA Statement of Position 94-3, *Reporting of Related Entities by Not-for-Profit Organizations*, or AICPA Audit and Accounting Guide, *Health Care Organizations*.

Why the FASB felt the need for special guidance concerning nonprofits

A major difference between combinations of nonprofit organizations and combinations involving only for-profit entities has important financial reporting connotations according to the FASB. Because a nonprofit organization lacks the type of ownership interests that business entities have, negotiations in nonprofit mergers and acquisitions focus on the furtherance of the public benefit and the mission of the entity, rather than on the returns for the owners. Many mergers and acquisitions by nonprofit entities do not involve a payment of consideration. In other words, many mergers and acquisitions by nonprofit organizations are not fair value exchanges but rather are nonreciprocal transfers. The FASB felt that that difference contributed significantly to the requirement that different accounting methods apply to a merger of nonprofit organizations and an acquisition by a nonprofit entity.

Mergers

Statement Number 164 requires the carryover method to account for a *merger of nonprofit entities*. A merger, in this regard, is a combination in which the governing bodies of two or more nonprofit entities cede control of those entities to create a new nonprofit entity. Generally, under the carryover method, the combined entity's initial financial statements reflect the carryforward basis of assets and liabilities of the combining entities at the merger date.

Acquisitions

With respect to acquisitions, Statement Number 164 requires the acquisition method to account for an *acquisition by a nonprofit entity*. An acquisition is a combination in which a nonprofit acquirer secures control of one or more nonprofit activities or businesses. The acquisition method is the same as the acquisition method described in Statement 141(R), with consideration given to guidance on items unique to a nonprofit entity and the excluding guidance that is not relevant to the nonprofit acquirer. According to the [Accounting Standards Codification™](#) Section 805-10-05, the acquisition method requires all of the following steps:

- a. Identifying the acquirer
- b. Determining the acquisition date
- c. Recognizing and measuring the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree
- d. Recognizing and measuring goodwill or a gain from a bargain purchase.

The area that differs most from Statement 141(R) is the recognition of goodwill. Unlike business entities, some nonprofit organizations are mostly supported by contributions and investments earnings. Others are more “businesslike,” and receive most of their support from service charges. In general, the more businesslike a nonprofit organization, the more relevant is information about the value of goodwill. However, Statement Number 164 recognizes that information about goodwill may be of limited use to donors in their assessments of a not-for-profit entity. Accordingly, Statement 164 requires an acquirer to account for goodwill as a separate charge against earnings. In other words, goodwill should not be recognized as an asset.

Disclosures

With regard to disclosures, Statement Number 164 addresses mergers and acquisitions separately. The Statement identifies specific requirements under each type of transaction.

Content of Statement 164

Statement Number 164 is 245 pages long. Much of the guidance covers implementation and sets forth specific examples. In addition, the Statement amends other literature including but not limited to:

- ARB No. 51, *Consolidated Financial Statements*
- FASB Statement No. 109, *Accounting for Income Taxes*
- FASB Statement No. 141 (revised 2007), *Business Combinations*
- FASB Statement No. 142, *Goodwill and Other Intangible Assets*
- FASB Statement No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*
- FASB Statement No. 157, *Fair Value Measurements*
- FASB Statement No. 160, *Non-controlling Interests in Consolidated Financial Statements*
- *FASB Interpretation No. 21, Accounting for Leases in a Business Combination*
- *FASB Interpretation No. 26, Accounting for Purchase of a Leased Asset by the Lessee during the Term of the Lease*
- *FASB Interpretation No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*
- *FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes*
- *FASB Staff Position FAS 157-1, Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13*
- *EITF Issue No. 02-13, Deferred Income Tax Considerations in Applying the Goodwill Impairment Test in FASB Statement No. 142*
- *AICPA Audit and Accounting Guide, Health Care Organizations*
- *AICPA Audit and Accounting Guide, Not-for-Profit Organizations*

The Codification

Statement Number 164 and its effects have not yet been reflected in the [Accounting Standards Codification™](#). The Codification will be the only authoritative guidance effective July 1, 2009. Our recent publication entitled [The Codification – a major restructuring of U.S. GAAP](#) provides additional information.

We have only summarized some of the more important provisions of Statement Number 164. Managers of nonprofit organizations are encouraged to seek the advice of a qualified professional if they are contemplating a merger or an acquisition.

Questions may be addressed to Vincent Ruocco, LLC, CPA at 203.932.2931.

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