

In brief

The latest news in financial reporting



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At a glance

The FASB's new definition of a business will likely result in more acquisitions being accounted for as asset acquisitions.

FASB finalizes a new definition of a business

What happened?

On January 5, 2017, the FASB issued final guidance that revises the definition of a business. The definition of a business affects many areas of accounting (e.g., acquisitions, disposals, goodwill impairment, consolidation). According to feedback received by the FASB, application of the current guidance is commonly thought to be too complex and results in too many transactions qualifying as business combinations.

New guidance

When substantially all of the fair value of gross assets acquired is concentrated in a single asset (or a group of similar assets), the assets acquired would not represent a business. This introduces an initial required screen that, if met, eliminates the need for further assessment.

To be considered a business, an acquisition would have to include an input and a substantive process that together significantly contribute to the ability to create outputs. The new guidance provides a framework to evaluate when an input and a substantive process are present (including for early stage companies that have not generated outputs). To be a business without outputs, there will now need to be an organized workforce. The Board noted that outputs are a key element of a business and included more stringent criteria for sets without outputs.

Finally, the new guidance narrows the definition of the term "outputs" to be consistent with how it is described in Topic 606, *Revenue from Contracts with Customers*. Under the final definition, an output is the result of inputs and substantive processes that provide goods or services to customers, other revenue, or investment income, such as dividends and interest.

Transition

For public business entities with a calendar year end, the standard is effective in 2018. All other entities have an additional year. Early adoption is permitted.

The amendments can be applied to transactions occurring before the guidance was issued (January 5, 2017) as long as the applicable financial statements have not been issued. For example, a public company with a calendar year-end can apply the new guidance to transactions that occurred after its third quarter, but before filing of its 2016 Form 10-K.

Why is this important?

The changes to the definition of a business will likely result in more acquisitions being accounted for as asset acquisitions across all industries, particularly real estate, pharmaceutical, and oil and gas. Application of the changes would also affect the

accounting for disposal transactions. Refer to Table 9-1 in PwC's Business combinations and noncontrolling interests guide on CFODirect.com for a summary of the accounting differences between the acquisition of a business versus an asset.

The FASB's updated definition does not impact the SEC definition of a business used to determine whether historical financial statements and pro forma information is required in certain SEC filings.

What's next?

The new guidance is the first phase of a broader project. The second phase, expected to be finalized in early 2017, will clarify the guidance for partial sales and transfers of nonfinancial assets. In the third phase, the FASB is expected to revisit the accounting differences between asset and business acquisitions and disposals.

Questions?

PwC clients who have questions about this *In brief* should contact their engagement team. Engagement teams who have questions should contact the National Professional Services Group.

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