



Financial Accounting  
Standards Board

MINUTES



Financial Accounting  
Standards Board

**To:** Board Members

**From:** Choi (x446)

**Subject:** Minutes of the September 19, 2007 Board Meeting on Not-for-Profit Mergers and Acquisitions **Date:** October 5, 2007

**cc:** FASB: Bielstein, Golden, MacDonald, Bossio, Mechanick, Posta, Tamulis, Vessels, Tully, Bolash, Delmonico, Choi, Lott, Lapolla, Gabriele, FASB Intranet, Chookaszian, Polley, Klimek, Allen; GASB: Reese, Schermann; IASB: Leisenring

*The Board meeting minutes are provided for the information and convenience of constituents who want to follow the Board's deliberations. All of the conclusions reported are tentative and may be changed at future Board meetings. Decisions become final only after a formal written ballot to issue a final Statement, Interpretation, or FSP.*

Topic: Redeliberations: Potential Departures from the Acquisition Method

Basis for Discussion: Memorandum #4 dated September 6, 2007, and Memorandum #5 dated September 14, 2007

Length of Discussion: 9:10–10:00 a.m.

Attendance:

Board members present:	Herz, Batavick, Crooch, Linsmeier, Seidman, Smith, and Young (by phone)
Board members absent:	None
Staff in charge of topic:	Posta
Other staff at Board table:	Bielstein, Bossio, Choi, Delmonico, Mechanick (by phone)
Outside participants:	None

### Summary of Decisions Reached:

As part of the redeliberations of the October 2006 Exposure Draft, *Not-for-Profit Organizations: Mergers and Acquisitions*, the Board reached the following decisions:

1. The Board decided that a merger is different from an acquisition and, therefore, a different accounting treatment for mergers would be appropriate. The Board agreed that the feature that distinguishes a merger is control—in a merger, the governing bodies of two or more not-for-profit organizations cede control of those organizations to create a new organization. In an acquisition, one organization obtains control over the net assets of another organization or business.
2. The Board affirmed that the acquisition method should be required for acquisitions by not-for-profit organizations. The Board decided that the carryover method of accounting should be retained for mergers between not-for-profit organizations. The Board considered but rejected suggestions that it also permit use of the carryover method of accounting for acquisitions by smaller not-for-profit organizations.
3. The Board directed the staff to draft a limited revision of the Exposure Draft to distinguish between a merger and an acquisition by a not-for-profit organization.

### Objective of Meeting:

The purpose of this meeting was to consider two issues that involve the method of accounting that should be applied to certain mergers and acquisitions by not-for-profit organizations:

1. Whether to affirm the proposed requirement in the Exposure Draft to apply the acquisition method to all mergers and acquisitions by a not-for-profit organization or to consider an alternative method for not-for-profit mergers.
2. Whether to permit the use of the carryover method of accounting for mergers and acquisitions by certain “small” not-for-profit organizations without public debt based on cost-benefit or other considerations.

Those issues are part of the Board’s redeliberations of the Exposure Draft.

### Matters Discussed and Decisions Reached:

#### **Issue 1A: Alternative Method of Accounting for Not-for-Profit Mergers**

1. Ms. Posta summarized the events and discussions that lead to the possibility of considering a distinction between mergers and acquisitions by not-for-profit organizations. Respondents to the Exposure Draft generally supported the improvements associated with the application of the acquisition method by not-for-profit organizations for many transactions. However, many respondents to the

Exposure Draft and participants in the March 2007 roundtable meeting expressed significant concerns about applying the Exposure Draft's proposed acquisition method to "true mergers" between not-for-profit organizations. For the purposes of discussion, the staff used the term *mergers* to describe transactions in which the governing bodies of two or more not-for-profit organizations cede control of those organizations to create a new organization.

2. Based on the concerns raised about mergers between not-for-profit organizations, Ms. Posta posed two questions for the Board's consideration:
  - a. Whether not-for-profit acquisitions and mergers are economically different transactions and, if so;
  - b. Whether those differences should result in different accounting methods.

#### **Issue 1A Staff Observation**

3. Ms. Posta observed that not-for-profit mergers seem to be different from acquisitions, based on the information received to date. A merger seems like the formation of a new entity, whereas the latter is an acquisition of the net assets of a business or of an entire organization by another not-for-profit organization. The fresh-start method seems to be conceptually preferable in terms of faithfully representing the formation of a new entity.

#### **Issue 1A Board Observation**

4. Board members generally agreed with the staff's observations in concept.

#### **Issue 1A Board Comments**

5. Ms. Seidman explained that based on previous discussions she believes that not-for-profit mergers occur when both entities cede control to form a new organization. The Board previously established its belief that a change in control is a significant economic event. She observed that an arrangement in which both parties cede control is very different from one in which one party cedes control while another gains control. She concluded that that difference provides an appropriate basis to account for a merger differently than an acquisition. Furthermore, she explained that

conceptually the fresh-start method seems to be the best way to account for a not-for-profit merger.

6. While Mr. Linsmeier did not object to distinguishing mergers from acquisitions by not-for-profit organizations, he observed that similar circumstances surrounding mergers and other transactions exist outside the not-for-profit sector. Mr. Herz stated that the Board should not be precluded from addressing the application of the fresh-start method to mergers by not-for-profit organizations simply because the conclusions reached might have implications that extend into other areas. He observed that although similar conditions exist in the for-profit sector, mergers occur much more frequently in the not-for-profit sector. Mr. Bossio also encouraged Board members not to impose the application of the acquisition method to events that it believes are truly not acquisitions. He also observed that the application of the fresh-start method would be consistent with the accounting for two gifts of entire organizations to a new organization.

#### **Issue 1B: How to Proceed with the Not-for-Profit Mergers and Acquisitions Project**

7. Ms. Posta then asked the Board to consider how to proceed with this project. Specifically, the question posed was whether to consider the application of the fresh-start method to mergers by not-for-profit organizations as part of this project. The Board meeting audience handout (attached) includes a chart with various alternatives on how the project could be conducted.

#### **Issue 1B Staff Recommendation**

8. Ms. Posta observed that some staff members support alternatives that would require the application of the fresh-start method to a not-for-profit merger because they believe that that method provides representationally faithful and relevant information to external users. Those staff members have a variety of views about how to conduct the project (some support Alternatives B, D, or E). Those alternatives would not preclude the Board from pursuing a comprehensive project on the fresh-start method in the future. The staff acknowledged that there are many other agenda priorities that currently need to be weighed by the Board in determining whether to conduct this exploration, which would be limited to not-for-profit mergers.

9. Ms. Bielstein supports, for purely practical reasons, that the Board not explore the fresh-start method for not-for-profit mergers as part of this project. Instead, she prefers a phased approach that would finish the not-for-profit project first and require the application of the acquisition method to all mergers and acquisitions by a not-for-profit organization, followed by a separate effort in the future to deal with fresh-start issues (either for the not-for-profit sector only or broadly).
10. If a majority of the Board does not support exploring the application of the fresh-start method to mergers by not-for-profit organizations as part of this project, staff members stated that they are not opposed to Alternative A<sup>1</sup> as an interim solution. That interim solution would basically maintain the status quo for mergers until the Board decides to address the fresh-start method comprehensively in the future. Under that alternative, the Board would issue a single final standard that addresses both not-for-profit mergers and acquisitions. An acquisition by a not-for-profit organization would be accounted for under the acquisition method, as proposed in the Exposure Draft, while the carryover method of accounting would be retained for mergers between not-for-profit organizations.

#### **Issue 1B Board Vote**

11. The Board voted in favor of Alternative A<sup>1</sup>. [Four Board members agreed (RHH, GJB, LFS, and LWS); three did not (GMC, TJL, and DMY).]

#### **Issue 1B Board Comments**

12. Mr. Crooch stated he would likely submit an alternative view to the limited revision to the Exposure Draft. He raised concerns that providing an alternative accounting method for mergers with perceived benefit to preparers (the carryover method) would motivate preparers to attempt to structure acquisitions to appear as if they are mergers. He added that similar to the criteria for the pooling-of-interests method in APB Opinion No. 16, *Business Combinations*, the Board would receive numerous requests to issue additional application guidance that further establishes the criteria and tests needed to identify when the carryover method would be required. He believes that it is too difficult for the Board to establish the criteria that constitutes a

merger and, therefore, he supports issuing a final Statement that requires the application of the acquisition method to all mergers and acquisitions by not-for-profit organizations (Alternative A).

13. Ms. Posta and Mr. Bossio responded that the limited revision to the Exposure Draft would expose the distinction between a merger and an acquisition for public comment. One of the goals of the exposure process would be to solicit input about the operability of a new principle for that distinction that focuses exclusively on a control criterion. That is, in a merger the governing bodies of two or more not-for-profit organizations each cede control of those organizations to create a new organization, whereas in an acquisition one organization obtains control over the net assets of another organization or business. That principle aims to evaluate events that are truly economically different and to avoid numerous rules that may not distinguish between economically different transactions.

14. Mr. Herz responded that he also shares Mr. Crooch's concerns about numerous requests to issue additional application guidance, similar to the pooling-of-interests guidance. However, he noted that retaining the carryover method for not-for-profit mergers was different because it is based on a single criterion, rather than 13 criteria as was the case for the pooling-of-interests method. He agreed that the comment letters will help in determining whether the principle that distinguishes a merger from an acquisition is operational or whether there should be additional criteria.

15. Ms. Bielstein acknowledged that the application of the carryover method to mergers puts more pressure on the principle. However, she reiterated her view that pursuing the fresh-start method is not a viable option within this project and would delay significant improvements in the financial reporting of not-for-profit organizations. Ms. Posta also explained that the current guidance under the relevant AICPA Audit and Accounting Guides and Opinion 16 is actually perceived to provide more of a choice to which accounting method can be selected (the purchase method or the pooling-of-interests method), and that the proposed guidance would provide more rigor than what is currently present in the not-for-profit sector.

16. Mr. Crooch suggested that, as an alternative, he would be willing to provide an option to not-for-profit organizations to apply the fresh-start method, rather than the acquisition method, to a merger or acquisition. Ms. Seidman objected to the introduction of choice between the acquisition method and the fresh-start method because offering a choice undermines the current accounting model. That is, this suggestion implies that (a) presumptively all assets and liabilities should be measured at fair value and (b) the financial statements could be remeasured any time a significant event occurs. Ms. Seidman does not yet support those implications at this time because they are integral to the Board's consideration of measurement attributes within the measurement phase of the conceptual framework.
17. Mr. Herz stated that he is less convinced that the fresh-start method is necessarily the best conceptual answer to the accounting for a merger. Contrary to many of the Board's assumptions regarding the usefulness of fresh-start accounting, he believes that users of financial statements in both the for-profit and the not-for-profit sectors ignore fair value measurements and subsequent charges to certain assets that result from the combination. He commented that the Board needs to address certain questions in the measurement phase of the conceptual framework project before it can determine the appropriateness of a one-time fair value revaluation of an entity. Specifically, he believes the questions of which measurement attribute should be used and when should be addressed more broadly before the fresh-start method is applied to this project. However, in the interim, it is clear to him that the acquisition method is absolutely the wrong answer for mergers. Therefore, he voted for Alternative A<sup>1</sup> in order to prevent delaying the correct accounting for the bulk of transactions that are considered acquisitions.
18. Ms. Seidman agreed with Mr. Herz and also voted for Alternative A<sup>1</sup>. She observed that the principle to distinguish not-for-profit mergers could also apply to joint ventures (both in the for-profit and not-for-profit sectors). She concluded that the application of the fresh-start method to those transactions is an issue the Board must study in due course as part of its discussion in the measurement phase of the

conceptual framework, rather than addressing fresh-start for not-for-profit mergers as part of this project.

19. Ms. Seidman also commented on the pressure that might be placed on the principle distinguishing a merger from an acquisition if the carryover basis is retained for not-for-profit mergers. She believes this is an opportunity for the Board to issue a principle and avoid issuing additional application guidance on distinguishing a merger from an acquisition. In fact, she raised the possibility of including in the notice to recipients that the Board would consider eliminating the distinction for a merger altogether if adherence to the principle is impossible without detailed rules. She emphasized that the request from recipients should focus on constructive criticism of the principle (for example, whether the principle is vague or underdeveloped and suggestions to improve the principle).
20. Mr. Smith also agreed with Mr. Herz that the fair value of the net assets of both merging not-for-profit organizations may not necessarily be the most relevant measurement attribute. He believes the fresh-start method should be addressed globally in the for-profit sector, before requiring the application of that method by not-for-profit organizations. He observed that there is a diverse spectrum of not-for-profit organizations—some to which fair value would be a relevant measurement and others to which fair value may not be a relevant measurement. He agreed that mergers and acquisitions by not-for-profit organizations are different economic transactions that should be accounted for differently, and therefore, he rejected Alternative A. He voted for Alternative A<sup>1</sup> because he is opposed at this time to adding a comprehensive project on the fresh-start method for practical reasons. Further, he disagreed that retaining the carryover method for not-for-profit mergers will be subjected to the same pressures as the pooling-of-interests method in the for-profit sector because the motivations are different.
21. Mr. Linsmeier observed that this issue is troublesome because each alternative has significant drawbacks. He agreed that the fresh-start method should be addressed comprehensively after the progression of the measurement phase of the conceptual



framework. Therefore, he opposed Alternatives B, C, D, and E. Mr. Linsmeier stated that he is unconvinced that either of the remaining alternatives (Alternative A or A<sup>1</sup>) is the correct step for not-for-profit mergers in the interim. The carryover method of accounting (Alternative A<sup>1</sup>) does not provide high-quality information about the new resulting entity to users going forward. Similarly, grossing up one merging organization's net assets to fair value under the acquisition method (Alternative A) does not provide useful information. Because he believes there will be significant tension in distinguishing a merger from an acquisition, he acquiesces to Alternative A. However, under Alternative A, he would add an accommodation for a merger between organizations without public debt to retain the carryover method.

22. Mr. Young voted for Alternative B because he believes that the fresh-start method provides the information that users of financial statements want. He added that the Board's discussion of the application of the fresh-start method should include questions surrounding the fair value of intangible assets. He observed that the tension in distinguishing a not-for-profit merger from an acquisition would be alleviated if the fresh-start method was required for mergers rather than the carryover method. Mr. Young also agreed with Mr. Crooch's suggestion to permit either the acquisition method or fresh-start method for not-for-profit mergers and acquisitions. He believes that the risk of organizations attempting to structure transactions to achieve a preferred method of accounting would be alleviated if the alternative method of accounting is the fresh-start method rather than the carryover method.

23. Mr. Batavick commented that one of the underlying reasons for considering an alternative accounting method for not-for-profit mergers was the highly questionable relevance to users of arbitrarily revaluing one side of a merger transaction. He believes that the ceding of control by both organizations is an event that is distinguishable from an acquisition. In his view, that distinction warrants a departure for mergers from the acquisition method of accounting. He affirmed that not-for-profit acquisitions should be accounted for under the acquisition method, and the Board should expedite that improvement. He agreed that the fresh-start method should be considered after the measurement phase of the conceptual framework

project. At this point the fresh-start method seems to be the best conceptual answer and could ultimately be the desired result. However, in the interim, the carryover method is better than the acquisition method when accounting for a merger. Therefore, Mr. Batavick voted for Alternative A<sup>1</sup>.

### **Issue 1C: Limited Revision of the Exposure Draft**

24. Based on the Board's decision to pursue Alternative A<sup>1</sup> in Issue 1B, the Board considered whether (and how) to expose the distinction between mergers and acquisitions by a not-for-profit organization for public comment.

### **Issue 1C Staff Recommendation**

25. The staff suggested that the most efficient plan would be to issue a limited revision to the Exposure Draft soon instead of waiting until the completion of redeliberations. That suggestion would allow for the redeliberations on the acquisition method concurrent with the exposure period. Additionally, based on the comments received on the Exposure Draft, the staff anticipates that there will not be additional issues that would require re-exposure; rather, there may be some considerations to scale-back on certain requirements for cost-benefit reasons.

### **Issue 1C Board Vote**

26. The Board unanimously agreed with the staff's suggestion to issue a limited revision to the Exposure Draft before completing the remaining redeliberations on the acquisition method. The Board directed the staff to begin drafting a limited revision of the Exposure Draft to distinguish between a merger and an acquisition by a not-for-profit organization. The staff plans to provide that draft to the Board (including a proposed basis for conclusions) for debate and/or affirmation at a future Board meeting.

### **Issue 2: "Small" Not-for-Profit Organizations without Public Debt**

27. The Exposure Draft proposes that all not-for-profit organizations apply the acquisition method to any merger or acquisition within the scope regardless of their size or primary source of support. Most respondents did not specifically address the

application of the proposed requirements to “small” not-for-profit organizations. However, a group of respondents, many of whom were represented at the roundtable meeting, suggested that small not-for-profit organizations without public debt be given the option of applying the carryover method rather than the acquisition method. Based on the Board’s decision on Issue 1 to retain the carryover method for not-for-profit mergers, Issue 2 would only apply to acquisitions by certain small organizations. The second issue is whether to permit the use of the carryover method for acquisitions by certain small not-for-profit organization without public debt based on the cost-benefit and other considerations.

## **Issue 2: Staff Recommendation**

28. The staff recommended that all not-for-profit organizations (large and small, public and nonpublic) be subject to the same requirements for the method of accounting. The staff disagrees with the assertions that the costs outweigh the benefits in an acquisition by a small nonpublic not-for-profit organization for three reasons:

- a. Use of the acquisition method for acquisitions better meets the needs of donors than does the carryover method because it provides information (1) that enables donors (as well as creditors) to assess an entity’s cash-generating abilities and cash flow potential in making allocation decisions and (2) with which to assess the organization’s ability to continue the mission and services of the consolidated organization for both present and potential donors
- b. Current values provide better information to help donors understand the expected resource inflows and outflows and an organization’s cost of providing services.
- c. The nature of the expected costs to apply the acquisition method is similar to the costs of applying other accounting requirements (such as donations of similar assets). Particularly, the incremental costs may not be that significant if the organizations undertake due diligence efforts, as those procedures often focus on current values.

29. Additionally, the staff recommended that permitting or requiring the use of the carryover method for acquisitions by small nonpublic not-for-profit organizations be rejected because:

- a. Generally, other asset acquisitions (including those that occur by gift) are required to be recognized at current exchange or fair values.

- b. Concerns about the ability to reliably determine the value of certain intangible assets (namely donor-related intangible assets) were shared by both small and large organizations.
- c. Current U.S. GAAP seldom provides exceptions to recognition and measurement requirements based on the size of the reporting organization.

**Issue 2 Board Vote**

30. Board members unanimously agreed with the staff's recommendation.

Follow-up Items:

None.

General Announcements:

None.



**Board Meeting Handout  
Not-for-Profit Mergers and Acquisitions  
September 19, 2007**

**PURPOSE**

1. As part of its redeliberations of the October 2006 Exposure Draft, *Not-for-Profit Organizations: Mergers and Acquisitions*, the Board will discuss:
  - a. Whether to further explore the possible use of a method of accounting other than the acquisition method for so-called “true mergers” or combinations in which an acquirer cannot be identified.
  - b. Whether to permit use of the carryover method of accounting for mergers and acquisitions by certain “small” not-for-profit organizations based on cost-benefit or other considerations.

**ISSUE 1: MERGERS BETWEEN NOT-FOR-PROFIT ORGANIZATIONS**

**Current Guidance**

2. AICPA Audit and Accounting Guides, *Health Care Organizations*, and *Not-for-Profit Organizations*, permit not-for-profit organizations to use the pooling method under certain circumstances. The Guides refer to the criteria in APB Opinion No. 16, *Business Combinations*, for determining which method of accounting to apply and provide an example of an acceptable application of the pooling method. The example given in the Guides hinges on whether there has been an exchange of consideration. Combinations by not-for-profit organizations with no exchange of consideration are permitted to be accounted for using the pooling method.

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The staff prepares Board meeting handouts to facilitate the audience's understanding of the issues to be addressed at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect the views of the FASB or its staff. Official positions of the FASB are determined only after extensive due process and deliberations.

3. An increase in the number of combinations in the health care industry led to a need to provide further guidance in the health care Guide on which method is appropriate for which combinations. Paragraph 11.38 of that Guide states:

. . . the guidance in APB Opinions No. 16 and No. 17 still apply and provides a useful framework when evaluating similar transactions entered into by not-for-profit health care business organizations. A list of possible factors to be considered when evaluating these transactions in relation to APB Opinion No. 16 is summarized as follows:

<u>Circumstances</u>	<u>Accounting and Disclosure Guidance</u>
Monetary consideration received or paid, change in legal title to assets, and/or assumption of liabilities.	This is similar to a purchase under APB Opinion No. 16.
Change in control (for example, change in sole corporate member).	This is similar to a pooling of interests transaction under APB Opinion No. 16. No step-up in basis.

[Footnote references omitted.]

4. Many mergers and acquisitions by not-for-profit organizations are currently accounted for in a manner similar to the pooling method, particularly those that occur without a transfer of consideration.

### **Proposed Guidance and Comments Received**

5. The Exposure Draft proposes that the acquisition method be applied to “any event that results in the initial recognition of another business or nonprofit activity (acquiree) in the financial statements of a not-for-profit organization.” Those transactions include what some have described as “true mergers.”

6. Overall, respondents supported the use of the acquisition method by not-for-profit organizations. However, many respondents to the Exposure Draft and participants in the March 2007 roundtable meeting expressed significant concerns about applying the Exposure Draft’s

proposed acquisition method to “true mergers” between not-for-profit organizations. Of the respondents that supported an alternative method of accounting for not for-profit mergers, more preferred the application of the fresh-start method to the carryover method.

- a. Those who preferred the fresh-start method for not-for-profit mergers believe that the resulting information would be more relevant for the new entity than would the carryover method or the acquisition method. Specifically, the use of the fresh-start method is consistent with the underlying principle that a new combined entity has been created that is separate from the two predecessors.
- b. Those who supported the carryover method for not-for-profit mergers believe that method appropriately treats the merging organizations consistently and gives commonality to the value of assets, while the acquisition method gives distorted information because it only revalues the assets and liabilities of one of the organizations.

7. The Board had small group meetings in April and in late July and early August 2007 to discuss those comments. Some of the comment letters also suggested factors that potentially could be used to identify not-for-profit mergers, including control, lack of an exchange of consideration, and commonality of mission. With input from resource group members, the staff further explored whether any one or more of those factors are the right ones—factors that distinguish the formation of a new merged entity from an acquisition. Based on that input, the staff developed the following working definition for discussion purposes. Terms that are currently defined in the Exposure Draft are in bold.

A merger or acquisition is any event that results in a **not-for-profit organization** initially recognizing an existing business or nonprofit activity (acquiree) in its financial statements. An organization may structure a merger or acquisition in a variety of ways for legal, taxation, or other reasons.

- a. A *merger* occurs when the governing bodies of two or more existing not-for-profit organizations cede control of those organizations and create a not-for-profit organization with a newly formed governing body.<sup>1</sup> None of the merging not-for-profit organizations retain or have direct or indirect control of the resulting not-for-profit organization.

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<sup>1</sup> The term *newly formed governing body* was used instead of *new organization* to encompass a broader notion. *New organization* implies a new legal corporation, whereas in some mergers the existing legal form of one of the merging organizations is used (with modifications) by the resulting organization. Using *newly formed governing body* would allow a reconstituted legal form that is a new economic entity, as well as a new legal organization to qualify as a merger if the other criteria are met.

- b. An *acquisition* occurs when a not-for-profit organization (the acquirer) obtains control of and initially recognizes a business or a nonprofit activity in its financial statements. An acquisition includes a combination in which a new organization is formed to effect the acquisition in which one of the combining entities that existed before the acquisition controls the resulting combined organization.

### Questions for the Board—Issue 1

8. The first issue is to consider what accounting method should be required for not-for-profit mergers and acquisitions as part of this project. Questions for the Board’s consideration follow:

**Question 1:** Are not-for-profit acquisitions different transactions from not-for-profit mergers?

**Question 2:** If yes, conceptually, should not-for-profit mergers be accounted for differently than not-for-profit acquisitions?

**Question 3:** If yes, should that different accounting be addressed as part of this project?

**Question 4:** If yes, should this project be conducted in two phases—first addressing not-for-profit acquisitions and then not-for-profit mergers?

**Question 5:** If yes, should the first phase of the project change the method of accounting for not-for-profit mergers in the meantime?

9. The following alternatives were identified for this issue:

**Alternative A:** Issue a single final Statement that requires the acquisition method be applied to “any event that results in the initial recognition of another business or nonprofit activity (acquiree) in the financial statements of a not-for-profit organization” (all not-for-profit mergers and acquisitions).

**Alternative A<sup>1</sup>:** Issue a single final Statement that requires the acquisition method be applied to acquisitions by not-for-profit organizations and that the carryover method of accounting be retained for not-for-profit mergers. (This was suggested at the September 12, 2007 education session.)

**Alternative B:** Issue a single final Statement that includes the accounting for both not-for-profit mergers and acquisitions and considers whether the fresh-start method should be applied to not-for-profit mergers.

**Alternative C:** Conduct the project in two phases—first addressing and finalizing the guidance for not-for-profit acquisitions and then not-for-profit mergers. Require in the first phase that not-for-profit mergers be accounted for using the acquisition method until the second phase is completed.

**Alternative D:** Conduct the project in two phases—first addressing and finalizing the guidance for not-for-profit acquisitions and then not-for-profit mergers. Require in the



first phase that not-for-profit mergers be accounted for using the carryover method unless the second phase unexpectedly stalls or stops, in which case, the acquisition method should apply.

**Alternative E:** Conduct the project in two phases—first addressing and finalizing the guidance for not-for-profit acquisitions and then not-for-profit mergers. Require in the first phase that not-for-profit mergers be accounted for using the carryover method until a Statement addressing the accounting for not-for-profit mergers is issued.

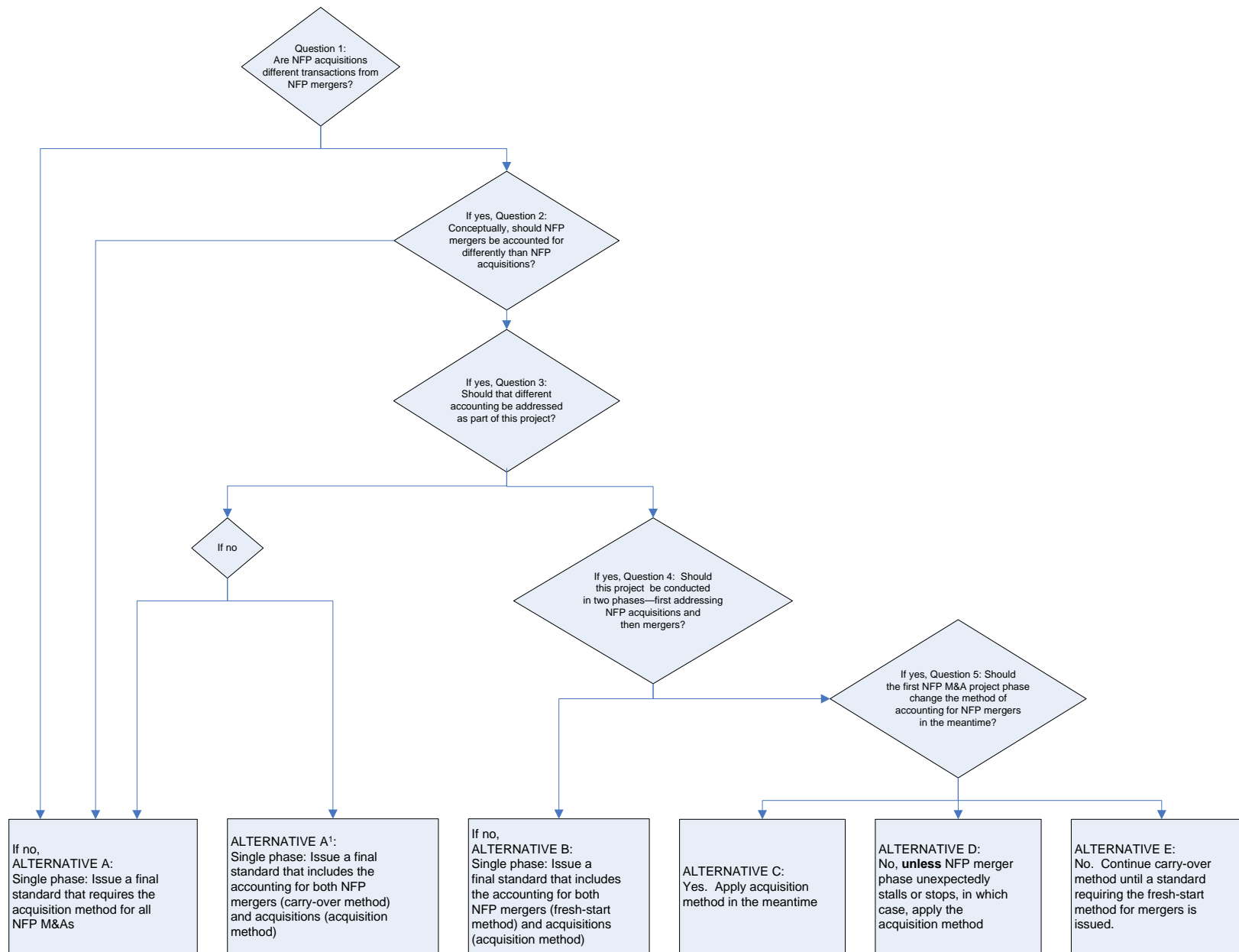
### **Staff Recommendation**

10. The staff believes that the fresh-start method for not-for-profit mergers is preferable in terms of representational faithfulness and relevance of the information to external users of that information. However, staff members have a variety of views about how to conduct the project. Some staff members support exploring the application of the fresh-start method to not-for-profit mergers as part of this project (Alternatives B, D, or E). That exploration would not preclude the Board from pursuing a comprehensive project on the fresh-start method in the future.

11. One staff member recommends, for purely practical reasons, that the Board not explore the fresh-start method for not-for-profit mergers as part of this project. She instead prefers a phased approach that would finish the not-for-profit project first, followed by a separate effort to deal with fresh-start issues (either for the not-for-profit sector only or broadly) (Alternatives A or C).

12. If a majority of the Board supports an alternative that distinguishes not-for-profit mergers from not-for-profit acquisitions, the staff supports exposing the distinguishing criterion for public comment. The staff believes that issuing a limited revision to the Exposure Draft concurrent with the redeliberations on the acquisition method would be the most efficient plan.

13. The following chart depicts how the Board's consideration of each question may lead to each project alternative.



## **ISSUE 2: “SMALL” NOT-FOR-PROFIT ORGANIZATIONS WITHOUT PUBLIC DEBT**

14. The second issue is whether the Board supports providing an alternative method of accounting for “small” not-for-profit organizations without public debt, such as requiring or permitting the carryover method of accounting. The Exposure Draft proposes that **all** not-for-profit organizations apply the acquisition method to any merger or acquisition within the scope, regardless of their size or primary source of support.

15. The primary reason that some constituents suggested that the Board consider this issue relates to cost-benefit considerations. Comments received said that the:

- a. Expected benefits of applying the acquisition method to small nonpublic not-for-profit organizations are outweighed by the expected costs to apply that method.
- b. Primary users of those not-for-profit organizations’ financial statements are donors and that the relevance of the information provided by the acquisition method is questionable, particularly in transactions with no exchange of consideration.
- c. Costs of applying the acquisition method should not be borne by those small organizations that generally have a lack of financial resources, limited financial expertise, and difficulty soliciting donations to pay for accounting costs.

### **Question for the Board—Issue 2**

16. The second issue will consider the following question:

**Question 1:** Does the Board support providing an alternative method of accounting for “small” not-for-profit organizations without debt?

### **Staff Recommendation**

17. The staff recommends that all not-for-profit organizations (large and small, public and nonpublic) be subject to the same requirements for the method of accounting. In considering the comment letters and the input received at the round table, the staff believes that the compelling cost-benefit case has not sufficiently been made to warrant a different accounting treatment based on “size.”