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APB ADOPTS OPINIONS ON BUSINESS COMBINATIONS (NO. 16) AND INTANGIBLE ASSETS (NO. 17)

On July 31st the Accounting Principles Board formally adopted new rules on accounting for corporate mergers. Other than the controversial size test which has been dropped, the new rules are substantially in accord with those informally approved by the Board last month (ARA Newsletter, June 29).

The Board had proposed restricting the "pooling of interests" method of accounting for business combinations to those in which combining companies are at least one ninth as large as each other. This restriction was dropped after further study. The Board did reaffirm limiting use of the method to combinations which are arranged through an exchange of common stock and which meet certain other restrictive conditions.

All other business combinations must be accounted for as purchases. Under this method the new rules require that goodwill -- any difference between the price paid and the value of tangible and identifiable intangible assets acquired -- be systematically written off against future earnings for a period not to exceed 40 years.

The new rules will be published by the Board within the next few weeks and will apply to mergers entered into after October 31, instead of August 31 as previously announced. This change will allow businessmen more time to become familiar with the new rules.

The following conditions must be met if pooling of interests accounting is to be used:

- Each of the combining companies is autonomous and independent and has not been a subsidiary or division of another corporation within two years before the plan of combination is initiated.

- The combination is effected in a single transaction or is completed according to a specific plan within one year.

- A corporation issues only common stock with rights identical to those of the majority of its outstanding voting common stock in exchange for substantially all of the voting common stock interest of another company.

- Each of the combining companies maintains substantially the same voting common stock interest; with no exchanges, retirements, or distributions to stockholders in contemplation of effecting the combination.

- Each of the combining companies reacquires shares of voting common stock only for purposes other than business combinations, and no company reacquires more than a normal number of shares after the date the plan of combination is initiated.

(continued)

o The ratio of the interest of an individual common stockholder to those of other common stockholders in a combining company remains the same as a result of the exchange of stock to effect the combination.

o The voting rights to which the common stock ownership interests in the resulting combined corporation are entitled are exercisable by the stockholders; the stockholders are neither deprived of nor restricted in exercising those rights.

o The combination is resolved at the date the plan is consummated and no provisions of the plan relating to the issue of securities or other considerations are pending.

o The combined corporation does not agree directly or indirectly to retire or reacquire all or part of the common stock issued to effect the combination.

o The combined corporation does not enter into other financial arrangements for the benefit of the former stockholders of a combining company, such as a guaranty of loans secured by stock issued in the combination, which in effect negate the exchange of equity securities.

o The combined corporation does not intend or plan to dispose of a significant part of the assets of the combining companies within two years after the combination except to eliminate duplicate facilities or excess capacity and those assets that would have been disposed of in the ordinary course of business of the separate company.

Under poolings it has been possible to include the profits of an acquired company in net income reported to stockholders even though the pooling took place after the end of the year reported on. This will now be prohibited.

INTANGIBLE ASSETS -- A corporation should record as assets the costs of intangible assets acquired from others, including goodwill acquired in a business combination. A corporation may record as assets the costs to develop identifiable intangible assets but should record as expenses the costs to develop intangible assets which are not specifically identifiable, such as goodwill. The cost of each type of intangible asset should be amortized from date of acquisition by systematic charges to income over the period estimated to be benefited. The period of amortization should not exceed 40 years.

EFFECTIVE DATE -- The provisions of the Opinions are effective for business combinations initiated after October 31, 1970 and apply to intangible assets recognized in those combinations or otherwise acquired after October 31, 1970. As defined in Opinion 16, date of initiation is the earlier of (1) the date the major terms of a plan, including the ratio of exchange of stock, are announced publicly or otherwise formally made known to the stockholders of any of the combining companies or (2) the date that stockholders of a combining company are notified in writing of an exchange offer.

NOTICE OF ANNUAL MEETING -- A meeting of the Board of Trustees and the annual meeting of the Accounting Research Association will be held on Sunday afternoon, September 20, 1970 between 2:00 and 4:00 P.M. in the Park Avenue North Room of the Waldorf-Astoria Hotel, New York, New York. Members and firm representatives of ARA in New York for the Institute's annual meeting are invited to attend the session between 3:00 and 4:00 P.M.