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## Accounting Research Association Newsletter, Volume IV, Number 5, May 12, 1971

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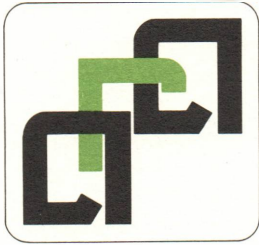
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# Accounting Research Association newsletter

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS, 666 FIFTH AVE., NEW YORK, N.Y. 10019

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Vol. IV, No. 5

May 12, 1971

## UNOFFICIAL INTERPRETATIONS TO BE ISSUED ON BUSINESS COMBINATIONS OPINION

At its May 5-7 meeting the Accounting Principles Board decided not to amend Opinion No. 16, Business Combinations. Instead, problems of intended application will be resolved through Unofficial Accounting Interpretations to be issued by the staff. Basic provisions of the interpretations, which will modify some of the proposals reported in the April 21 Newsletter, include the following:

- If substantially all of the shareholders of a successor company resulting from a transaction accounted for by the purchase method are not associated with the selling company, a subsequent business combination by the successor company, described in paragraph 46a, may be accounted for by the pooling of interests method.
- The parent company must own substantially all of a subsidiary's voting stock if the subsidiary is to be permitted to distribute voting common stock of the parent to effect a business combination as a pooling of interests. The parent company would also have to meet all the other conditions for pooling as if it had issued its own stock directly to effect the combination. Paragraph 46a indicates that this can be done only with respect to a wholly owned subsidiary, which the interpretation will define as meaning a subsidiary whose stock is substantially all owned by the parent.
- A pooling of interests would not be precluded by paragraph 47c and 47d if treasury stock were acquired earlier than two years before initiation of the combination or if such stock acquired within two years of initiation were sold or issued prior to consummation of the combination. Also, treasury stock not disposed of could be reserved for specific purposes existing at consummation. These reservations could include shares for grants under stock option or compensation plans, stock dividends declared, initiated business combinations which are to be accounted for as purchases, and contingent shares to be issued for prior business combinations.
- A disposition of a significant part of the assets of a company prior or subsequent to a combination accounted for as a pooling of interests will not violate paragraph 47c or 48c if the disposition is made to comply with an order of a governmental body, or if, on the basis of available evidence, it would avoid such an order.
- Disclosure of the financial effects of a combination consummated after the balance sheet date, but before the financial statements are issued, need not be confined to the notes, but may be presented otherwise as supplemental information in the financial statements.

(continued)

### TWO CLASS METHOD OF COMPUTING EARNINGS PER SHARE

The forthcoming Unofficial Accounting Interpretation will state that the two class method in computing primary earnings per share should be used for real estate investment trusts which elect, under the Internal Revenue Code, to pay dividends equal to 90% or more of earnings. (See ARA Newsletter, April 21, 1971.) In these cases the use of proceeds from the exercise of warrants, as provided under paragraph 38 of Opinion No. 15, should be assumed, as well as allocation of earnings for distributions to security holders.

### HEARING ON MARKETABLE SECURITIES

Some 20 people have asked to appear and 40 individuals and organizations have indicated they will present written statements in connection with the APB's public hearing on marketable equity securities to be held in New York on May 25-26. (See ARA Newsletter, March 17, 1971.) All interested persons are invited to attend this discussion on whether investments in the voting stock of another company should be accounted for at current market value or at historical cost. Further information can be obtained from the APB Administrative Director's office at the Institute.

### TAX DIVISION TESTIFIES ON PROPOSED TREASURY REGULATIONS

In oral and written testimony before a Treasury Department hearing on May 11 representatives of the Institute's Tax Division stated their opposition to a key provision of the proposed regulations on accounting for long term contracts.

This provision, Sec. 1.451-3(e)(1) would permit the completed contract method to be used only if the taxpayer uses such a method in reports to shareholders, creditors, etc.

At its May 7 meeting the Institute's Board of Directors authorized a reexamination of Institute policy in view of the Treasury Department's apparent change in approach which would require financial accounting to conform with tax accounting in many cases.

### PILOT QUALITY REVIEW PROGRAM ESTABLISHED

Guidelines for post audit quality review of work papers have been field tested and the committee is ready to arrange reviews for interested members.

The plan is to have two reviewers spend two days in the practitioner's office discussing several engagements selected by the practitioner. Reviews conducted this summer will be used as a basis for recommendations to Council in September on the future of the service.

For further information about the program, contact Ed Musho of the Technical Services Division.