November 2025

On the Radar
Business Combinations

Entities engage in acquisitions for various reasons. For example, they may be looking to grow in size, diversify their product offerings, or expand into new markets or geographies.

The accounting for acquisitions can be complex and begins with a determination of whether an acquisition should be accounted for as a business combination. ASC 805-10, ASC 805-20, and ASC 805-30 address the accounting for a business combination, which is defined in the ASC master glossary as "[a] transaction or other event in which an acquirer obtains control of one or more businesses." Typically, a business combination occurs when an entity purchases the equity interests or the net assets of one or more businesses in exchange for cash, equity interests of the acquirer, or other consideration. However, the definition of a business combination applies to more than just purchase transactions; it incorporates all transactions or events in which an entity or individual obtains control of a business.

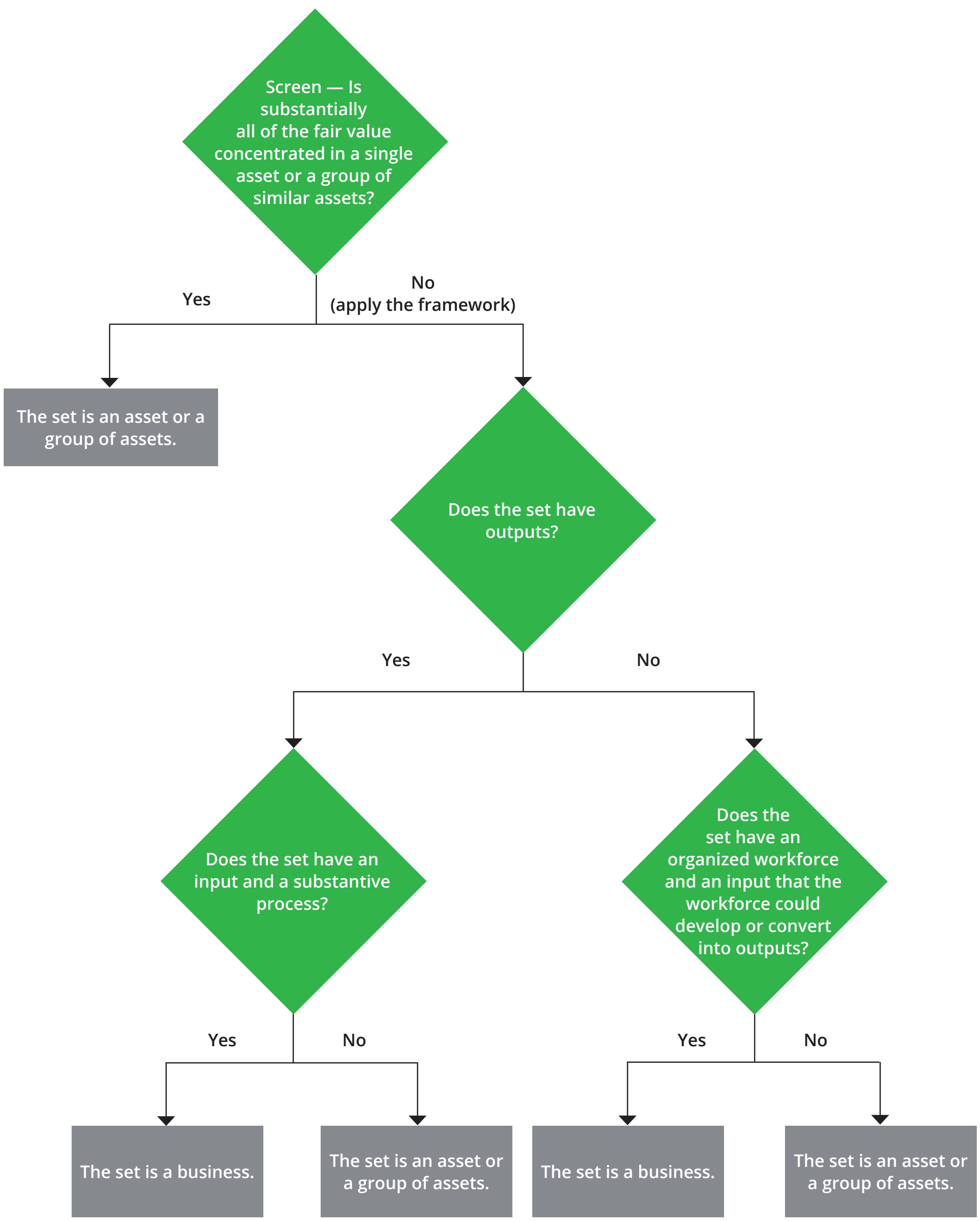
If the acquisition does not meet the definition of a business combination, the entity must determine whether it should be accounted for as an asset acquisition under ASC 805-50. Distinguishing between the acquisition of a business and the acquisition of an asset or a group of assets is important because there are many differences between the accounting for each. Alternatively, if the assets acquired consist of primarily cash or investments, the substance of the transaction may be a capital transaction (a recapitalization) rather than a business combination or an asset acquisition.

Determining Whether an Acquisition Is a Business Combination or an Asset Acquisition

To determine whether an acquisition should be accounted for as a business combination, an entity must evaluate whether the acquired set of assets and activities together meet the definition of a business in ASC 805.

An entity first uses a "screen" to assess whether substantially all of the fair value of the gross assets acquired is concentrated in a single identifiable asset or group of similar identifiable assets. If the screen is not met, the entity must apply a "framework" for determining whether the acquired set includes, at a minimum, an input and a substantive process that together significantly contribute to the ability to create outputs. If so, the acquired set is a business.

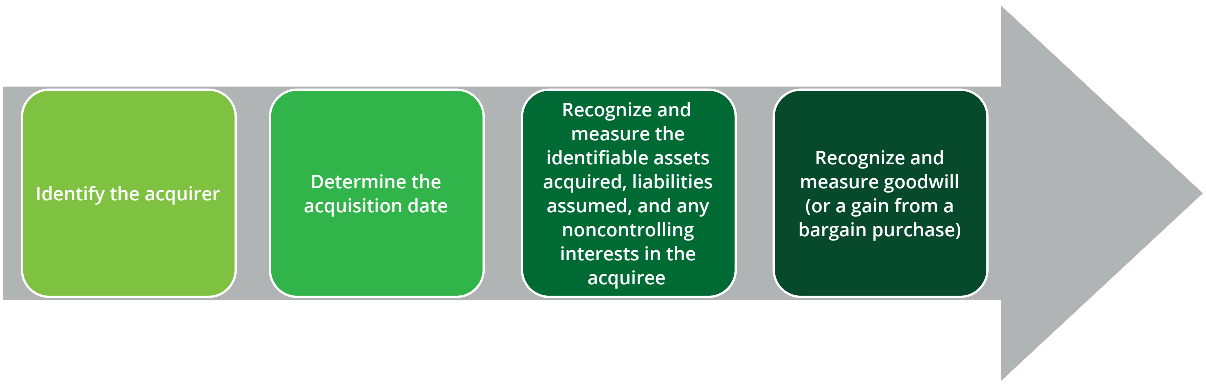
The decision tree below illustrates how to determine whether an acquisition represents a business combination or an asset acquisition.



SEC registrants are required to use the definition of a business in SEC Regulation S-X, Rule 11-01(d), when evaluating the requirements of SEC Regulation S-X, Rule 3-05, and SEC Regulation S-X, Article 11. The definition of a business in Rule 11-01(d) is different from the definition of a business in ASC 805-10.

Business Combinations

ASC 805 requires an entity to account for a business combination by using the acquisition method of accounting. Application of the acquisition method requires the following steps:



STEP 1 Identify the Acquirer

The first step of applying the acquisition method is identifying the acquirer. ASC 805-10-25-4 requires entities to identify an acquirer in every business combination. Before adoption of ASU 2025-03, the ASC master glossary defines an acquirer as follows:

> The entity that obtains control of the acquiree. However, in a business combination in which a variable interest entity (VIE) is acquired, the primary beneficiary of that entity always is the acquirer.

The entity identified as the acquirer for accounting purposes usually is the entity that transfers the consideration (e.g., cash, other assets, or its equity interests) to effect the acquisition. However, when a business combination is effected primarily by exchanging equity interests, the determination of which entity is the acquirer requires careful evaluation of the relevant facts and circumstances. In some cases, the entity that issues its equity interests (the "legal acquirer") is determined for accounting purposes to be the acquiree (also called the "accounting acquiree"), while the entity whose equity interests are acquired (the "legal acquiree") is for accounting purposes the acquirer (also called the "accounting acquirer"). Such transactions are commonly called reverse acquisitions.

If the entity identified as the accounting acquiree meets the definition of a business, the accounting acquirer accounts for the acquisition as a business combination in accordance with ASC 805. However, if the entity identified as the accounting acquiree has no substantive assets other than cash and investments, the nature of the transaction may be a reverse recapitalization.

Changing Lanes

On May 12, 2025, the FASB issued ASU 2025-03, which revises the guidance in ASC 805 on identifying the accounting acquirer in a business combination in which the legal acquiree is a VIE. The ASU is intended to improve comparability between business combinations that involve VIEs and those that do not.

Before adoption of ASU 2025-03, ASC 805-10-25-5 states that in a business combination in which a VIE is acquired, the primary beneficiary of the legal acquiree is always the accounting acquirer. Conversely, for a business combination in which the acquired entity is determined not to be a VIE and it is not clear which of the combining entities is the acquirer after applying the voting interest entity (VOE) model, a reporting entity is required to consider the factors in ASC 805-10-55-11 through 55-15 when determining which legal entity is the accounting acquirer. As a result, in an acquisition transaction effected primarily by exchanging equity interests, a reporting entity may reach different conclusions related to determining the accounting acquirer in a business combination involving a legal acquiree that is a VIE than in a combination in which the legal acquiree is a VOE. That is, having considered the factors in ASC 805-10-55-12 through 55-15, a reporting entity might not identify the primary beneficiary of the legal acquiree that is a VIE as the accounting acquirer of the combining entities.

The identification of the accounting acquirer establishes which entity in the business combination will have its assets and liabilities remeasured in accordance with ASC 805-20 (generally at fair value) and creates a new basis of accounting. Accordingly, the comparability of similar transactions under existing GAAP can be greatly affected by the structure of the legal acquiree and whether such entity qualifies as a VIE or a VOE.

ASU 2025-03 is effective for fiscal years beginning after December 15, 2026, including interim periods within those fiscal years. Early adoption is permitted. The amendments in ASU 2025-03 must be applied prospectively to any business combination that occurs after the initial adoption date.

STEP 2 Determine the Acquisition Date

The second step of applying the acquisition method is determining the acquisition date. The acquisition date is the date on which control of the business transfers to the acquirer and generally coincides with the date on which the acquirer legally transfers the consideration to the seller, receives the assets, and incurs or assumes the liabilities (i.e., the closing date). However, in unusual circumstances, the acquisition date can be before or after the closing date.

Determining the acquisition date is important because on this date:

- The consideration transferred is measured at fair value as the sum of (1) the assets transferred by the acquirer, (2) the liabilities incurred by the acquirer to former owners of the acquiree (e.g., contingent consideration), and (3) the equity interests issued by the acquirer.
- The assets acquired, liabilities assumed, and any noncontrolling interests are identified and measured.
- The acquirer begins consolidating the acquiree, if required.

STEP 3 Recognize and Measure the Identifiable Assets Acquired, Liabilities Assumed, and Any Noncontrolling Interests in the Acquiree

The third step of applying the acquisition method is recognizing and measuring the identifiable assets acquired, liabilities assumed, and any noncontrolling interests in the acquiree. Step three is based on two key principles, which ASC 805 calls the recognition principle and the measurement principle. Under the recognition principle in ASC 805-20-25-1, an acquirer must "recognize, separately from goodwill, the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree." As a result of applying the recognition principle, an acquirer may recognize certain assets and liabilities that were not previously recognized in the acquiree's financial statements, such as certain intangible assets.

Under the measurement principle in ASC 805-20-30-1, an acquirer is required to measure "the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree at their acquisition-date fair values." Thus, most assets and liabilities and items of consideration are measured at fair value in accordance with the principles of ASC 820.

ASC 805 does include exceptions to its recognition and fair value measurement principles, such as for deferred taxes, employee benefits, share-based payments, and assets held for sale. Such exceptions are recognized and measured in accordance with other applicable GAAP rather than the general principles discussed in ASC 805.

STEP 4

Recognize and Measure Goodwill (or a Gain From a Bargain Purchase)

The fourth and final step in applying the acquisition method is recognizing and measuring goodwill or a gain from a bargain purchase. The ASC master glossary, as amended by ASU 2023-05, defines goodwill as "[a]n asset representing the future economic benefits arising from other assets acquired in a business combination, acquired in an acquisition by a not-for-profit entity, or recognized by a joint venture upon formation that are not individually identified and separately recognized." Because goodwill is not a separately identifiable asset, it cannot be measured directly. It is therefore measured as a residual and calculated as the excess of the sum of the following items over the net of the acquisition-date values of the identifiable assets acquired and the liabilities assumed: (1) the consideration transferred, (2) the fair value of any noncontrolling interest in the acquiree if a less than 100 percent interest in the acquiree is acquired, and (3) the fair value of the acquirer's previously held equity interest in the acquiree if the acquirer had a noncontrolling equity interest in the acquiree before the acquisition. Occasionally, the sum of (1) through (3) above is less than the net of the acquisition-date fair values of the identifiable assets acquired and the liabilities assumed. In such a case, the acquirer recognizes a gain, referred to as a bargain purchase gain, in earnings on the acquisition date.

Because it may take time for an entity to obtain the information necessary to recognize and measure all the items exchanged in a business combination, the acquirer is allowed a period in which to complete its accounting for the acquisition. That period — referred to as the measurement period — ends as soon as the acquirer (1) receives the information it had been seeking about facts and circumstances that existed as of the acquisition date or (2) learns that it cannot obtain further information. However, the measurement period cannot be more than one year after the acquisition date. During the measurement period, the acquirer recognizes provisional amounts for the items for which the accounting is incomplete.

Under ASC 805-10-55-16, the acquirer is required to recognize any adjustments to the provisional amounts that were recognized during the measurement period "in the reporting period the adjustments are determined." The adjustments are calculated as if the accounting had been completed on the acquisition date. When an acquirer adjusts a provisional amount, the offsetting entry generally increases or decreases goodwill but may also result in adjustments to other assets and liabilities. Measurement-period adjustments may also affect the income statement. In accordance with ASC 805-10-25-17, an acquirer must recognize, in the reporting period in which the adjustment amounts are determined (rather than retrospectively), the "effect [on earnings] of changes in depreciation, amortization, or other income effects . . . if any, as a result of the change to the provisional amounts calculated as if the accounting had been completed at the acquisition date."

Other Related Issues

Pushdown Accounting

When an entity obtains control of a business, a new basis of accounting is established in the acquirer's financial statements for the assets acquired and liabilities assumed. ASC 805-10, ASC 805-20, and ASC 805-30 provide guidance on accounting for an acquisition of a business in the acquirer's consolidated financial statements.

Sometimes the acquiree in a business combination will prepare separate financial statements after the acquisition. In such cases, the acquiree has the option of whether to use the parent's basis of accounting or the acquiree's historical carrying amounts for the assets acquired and liabilities assumed in its separate financial statements. Use of the acquirer's basis of accounting in the preparation of an acquiree's separate financial statements is called "pushdown accounting."

An acquiree can elect to apply pushdown accounting in its separate financial statements each time another entity or individual obtains control of it. If it does not elect to apply pushdown accounting before the financial statements are issued (SEC filer) or are available to be issued (other entities), it may subsequently elect to apply pushdown accounting to its most recent change-in-control event in a later reporting period. However, such a later election would be a change in accounting principle and the acquiree would be required to apply the guidance on a change in accounting principle in ASC 250 in such circumstances, including all relevant disclosure requirements.

ASC 250-10-45-5 requires that an entity "report a change in accounting principle through retrospective application . . . to all prior periods" unless doing so would be impracticable. We would expect entities that elect pushdown accounting on a later date to apply it retroactively to the acquisition date since the parent generally would be expected to have maintained the records for all prior periods. Further, an SEC registrant that elects a voluntary change in accounting principle must file a preferability letter with the SEC.

While an entity can elect to apply pushdown accounting in a subsequent reporting period, it cannot reverse the application of pushdown accounting in financial statements that have been issued (SEC filer) or are available to be issued (other entities).

Common-Control Transactions

A common-control transaction is typically a transfer of net assets or an exchange of equity interests between entities under the control of the same parent. While a common-control transaction is similar to a business combination for the entity that receives the net assets or equity interests, such a transaction does not meet the definition of a business combination because there is no change in control over the net assets. Therefore, the accounting and reporting for a transaction between entities under common control is outside the scope of the business combinations guidance in ASC 805-10, ASC 805-20, and ASC 805-30 and is addressed in the "Transactions Between Entities Under Common Control" subsections of ASC 805-50.

Since there is no change in control over the net assets from the parent's perspective in a common-control transaction, there is no change in basis in the net assets. ASC 805-50 requires the receiving entity to recognize the net assets received at their historical carrying amounts, as reflected in the ultimate parent's financial statements.

Entities should also be aware that internal reorganizations could trigger a requirement to apply pushdown accounting. While common-control transactions are generally accounted for at historical cost, sometimes the carrying amounts of the transferred assets and liabilities in the ultimate parent's consolidated financial statements differ from the carrying amounts in the transferring entity's separate financial statements (e.g., if the transferring entity had not applied pushdown accounting). ASC 805-50-30-5 states that, in such cases, the receiving entity's financial statements must "reflect the transferred assets and liabilities at the historical cost of the parent of the entities under common control." We believe that the historical cost of the parent refers to the historical cost of the ultimate parent or controlling shareholder. Therefore, while the application of pushdown accounting is optional in the acquiree's separate financial statements, it may be required in certain cases after an internal reorganization.

Asset Acquisitions

The term "asset acquisition" is used to describe an acquisition of an asset, or a group of assets, that does not meet the definition of a business in ASC 805. An asset acquisition is accounted for in accordance with the "Acquisition of Assets Rather Than a Business" subsections of ASC 805-50 by using a cost accumulation model. In such a model, the cost of the acquisition, including certain transaction costs, is allocated to the assets acquired on a relative fair value basis and no goodwill is recognized. By contrast, in a business combination, the assets acquired are recognized generally at fair value and goodwill is recognized. As a result, there are significant differences between the accounting for an asset acquisition and the accounting for a business combination.

Joint Venture Formations

In August 2023, the FASB issued ASU 2023-05, under which an entity that qualifies as either a joint venture or a corporate joint venture as defined in the ASC master glossary is required to apply a new basis of accounting upon the formation of the joint venture. Under ASU 2023-05 (codified in ASC 805-60), the formation of a joint venture or a corporate joint venture (collectively, "joint ventures") results in the "creation of a new reporting entity," and no accounting acquirer is identified under ASC 805. Accordingly, a new basis of accounting would be established upon the formation date. A joint venture must initially measure its assets and liabilities at fair value on the formation date, which the ASU defines as "the date on which an entity initially meets the definition of a joint venture." Further, the excess of the fair value of a joint venture as a whole over the net assets of the joint venture is recognized as goodwill.

The amendments in ASU 2023-05 are effective for all joint ventures within the ASU's scope that are formed on or after January 1, 2025, and early adoption is permitted. Joint ventures formed on or after the effective date of ASU 2023-05 will be required to apply the new guidance prospectively. Joint ventures formed before the ASU's effective date are permitted to apply the new guidance (1) retrospectively, if they have "sufficient information" to do so, or (2) prospectively, if financial statements have not yet been issued (or made available for issuance). If retrospective application is elected, transition disclosures must be provided in accordance with ASC 250.

Purchased Financial Assets

In June 2023, the FASB issued a proposed ASU that would amend the guidance in ASU 2016-13 regarding the accounting upon the acquisition of financial assets acquired in (1) a business combination, (2) an asset acquisition, or (3) the consolidation of a VIE that is not a business. The proposed ASU would broaden the population of financial assets that are within the scope of the gross-up approach under ASC 326 by requiring an acquirer to apply the gross-up approach in accordance with ASC 805 to all financial assets acquired in a business combination rather than only to purchased financial assets with credit deterioration. For financial assets acquired as a result of an asset acquisition or through consolidation of a VIE that is not a business, the asset acquirer would apply the gross-up approach to seasoned assets, which are acquired assets unless the asset is deemed akin to an in-substance origination. A seasoned asset is an asset (1) that is acquired more than 90 days after origination and (2) for which the acquirer was not involved with the origination. Practitioners should monitor the proposed ASU for any developments that might change the current accounting.

On April 30, 2025, the Board decided to revise the project objective to improve the accounting for the acquisition of purchased financial assets, other than PCD assets, through narrow amendments. Under this revised project objective, the current accounting for PCD assets would be retained, and seasoned loan receivables, excluding credit cards, would be subject to the amendments to the final ASU. The Board directed the staff to draft a final Accounting Standards Update for vote by written ballot.

SEC Reporting Requirements

To ensure that investors receive relevant financial information about a company's significant activities, the SEC requires registrants to report financial information about significant acquired or to be acquired businesses or the acquisition of real estate operations (the acquiree) in certain filings under Regulation S-X, Rules 3-05 and 3-14, respectively.

See Deloitte's Roadmap *SEC Reporting Considerations for Business Acquisitions* for more information.

Deloitte's Roadmap *Business Combinations* provides Deloitte's insights into and interpretations of the guidance in ASC 805 on business combinations, pushdown accounting, common-control transactions, and asset acquisitions as well as an overview of related SEC reporting requirements.

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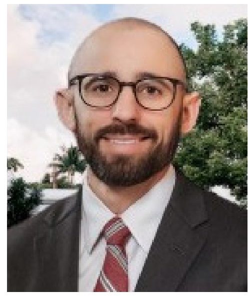

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