

Viewpoint

Identifying the acquirer in a
business combination

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Introduction

The accounting for business combinations, and specifically for identifying the accounting acquirer in such transactions, continues to be a challenging area to apply in U.S. GAAP, and the consequence of getting it wrong often results in a restatement.

The guidance in ASC 805 requires one of the combining entities in a business combination to be identified as the acquiring entity. That entity is then required to apply the acquisition method to account for the transaction under ASC 805. The acquisition method of accounting requires an acquirer to determine the acquisition date and to recognize and measure the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree, as well as any goodwill or gains derived from a bargain purchase.

Grant Thornton continues to navigate this challenging area of U.S. GAAP with our clients and, as a result, has outlined the applicable guidance in this publication, along with our insights and examples, to assist our clients and others in their analyses. This Viewpoint discusses how to identify the acquirer in business combinations that fall within the scope of ASC 805-10. It does not apply to transactions or events within the scope of ASC 805-50, which has its own discrete scope covering asset acquisitions, transactions between entities under common control, the formation of master limited partnerships, and pushdown accounting.

1. Overview of identifying the acquirer

Under the guidance in ASC 805-10-25-4, one of the combining entities in a business combination transaction must be identified as the acquirer. A business combination can have only one acquirer, even if there are multiple parties involved in the transaction. The Master Glossary in the FASB's Codification defines both the "acquirer" and the "acquiree" to facilitate the application of this guidance.

In May 2025, the FASB issued ASU 2025-03, *Determining the Accounting Acquirer in the Acquisition of a Variable Interest Entity (Business Combinations (Topic 805) and Consolidation (Topic 810))*. The amendments in ASU 2025-03 revise the definition of the term "acquirer" by modifying the guidance for determining the accounting acquirer in business combinations that involve a variable interest entity (VIE).

Prior to these amendments, the guidance in ASC 805 prescribed that the primary beneficiary of a VIE acquired in a business combination was always the accounting acquirer. Following the issuance of ASU 2025-03, however, the automatic assumption that the accounting acquirer is the primary beneficiary no longer applies in business combinations that are primarily effected through the exchange of equity interests in which a VIE is acquired. In such cases, entities must now evaluate additional factors in ASC 805 to determine the appropriate accounting acquirer, and, as a result, the accounting acquirer in these cases may be different from the determination made using legacy GAAP.

The amendments introduced by ASU 2025-03 are effective for all entities in annual reporting periods beginning after December 15, 2026, including interim periods within those annual periods. Early adoption is permitted in any interim or annual reporting period if the financial statements have not yet been issued or been made available for issuance. The guidance should be applied prospectively to all business combinations with an acquisition date occurring on or after the initial application date.

The Master Glossary definitions of "acquirer," both before and after the amendments, as well as the definition of "acquiree," are presented below.

Acquirer (pre-adoption of ASU 2025-03): 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.

Acquirer (post-adoption of ASU 2025-03): The entity that obtains control of the acquiree. See paragraphs 805-10-25-4 through 25-5 for guidance on determining the acquirer.

Acquiree: The business or businesses that the acquirer obtains control of in a business combination. This term also includes a nonprofit activity or business that a not-for-profit acquirer obtains control of in an acquisition by a not-for-profit entity.



ASC 805-10-25-4

For each business combination, one of the combining entities shall be identified as the acquirer.

The identification of the acquirer in a business combination begins with the guidance in ASC 810, which outlines how to consolidate an entity using two primary consolidation models: the *variable interest entity* (VIE) model and the *voting interest entity* (VOE) model. In performing an analysis of the accounting acquirer, a reporting entity should take these steps in the following prescribed order:

- (1) First, consider whether the transaction involves the acquisition of a VIE:
 - *Before the adoption of ASU 2025-03*: In a business combination involving the acquisition of a VIE, the entity identified as the primary beneficiary of the VIE is deemed to be the accounting acquirer, regardless of whether the transaction is effected primarily through the transfer of cash or the exchange of equity interests.
 - *After the adoption of ASU 2025-03*:
 - In a business combination involving the acquisition of a VIE that is effected primarily through the transfer of cash or other assets, the entity identified as the primary beneficiary is the accounting acquirer.
 - In a business combination involving the acquisition of a VIE that is effected primarily through the exchange of equity interests, entities are required to assess the factors set forth in ASC 805-10-55-12 through 55-15 to determine the accounting acquirer.
- (2) Second, if the VIE subsections of ASC 810 do not apply, entities must consider whether the VOE model in the general subsections of ASC 810 clearly identifies the accounting acquirer.
- (3) Third, if the VIE subsections of ASC 810 do not apply and the guidance in ASC 810 does not clearly indicate which of the combining entities is the acquirer, then entities must consider the additional guidance in ASC 805-10-55-11 through 55-15 to identify the acquirer for accounting purposes.

A business combination effected primarily by an exchange of equity interests between the combining entities, or between two or more combining entities with a newly established entity formed for the purpose of the business combination (as discussed in Section 3.4), is an example of when the guidance in ASC 810 may not clearly identify the accounting acquirer.

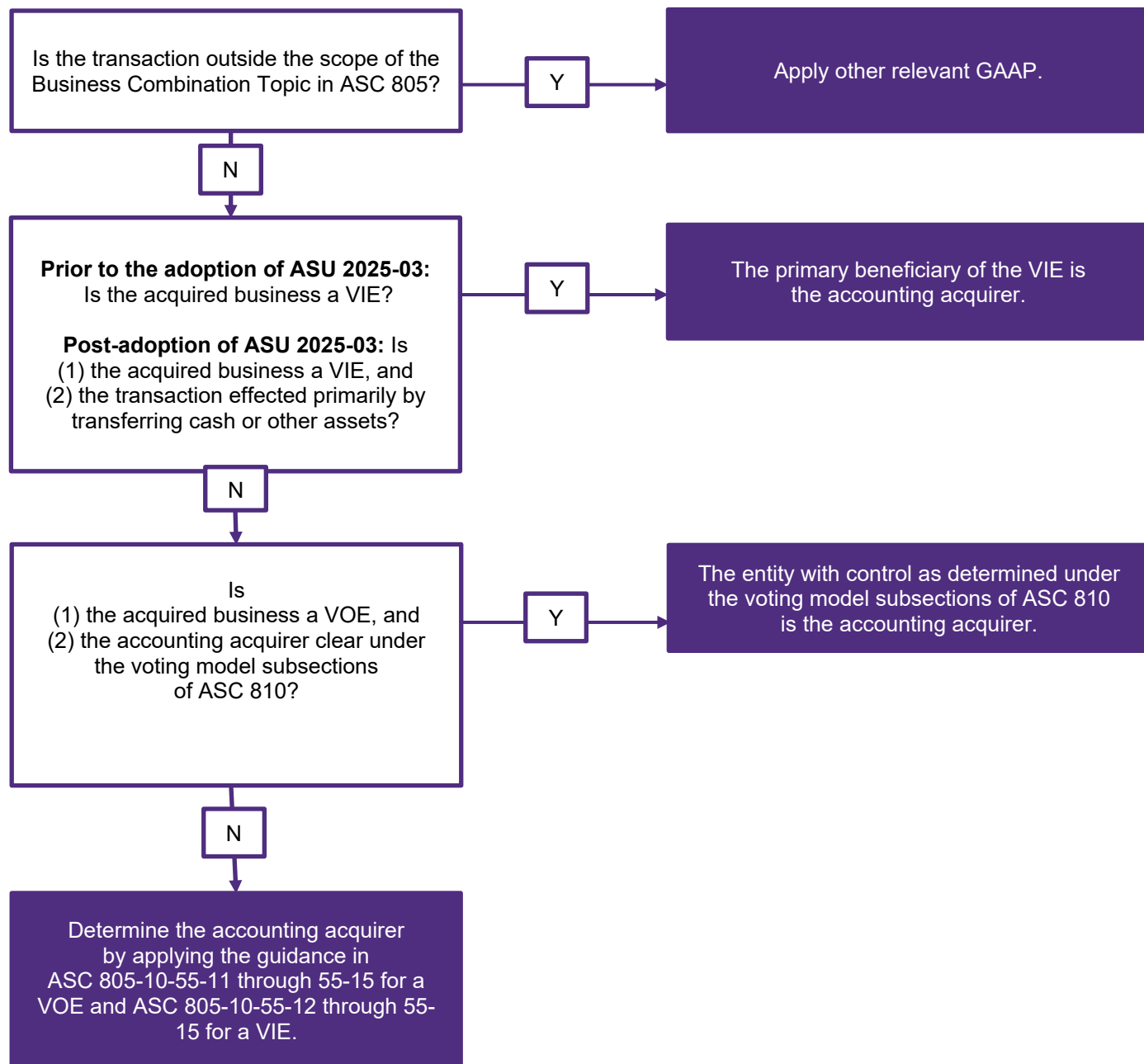


Grant Thornton insight: Transactions effected 'primarily' by exchanging equity interests

ASC 805 does not provide guidance for determining when a transaction is effected "primarily" by exchanging equity interests. As a result, entities will need to apply judgment to determine whether the transaction was effected primarily by the exchange of equity interests for those transactions involving an exchange of both equity interests and cash payments to the selling shareholders. In making this determination, an entity may consider factors such as the relative value of the equity interests and cash exchanged.

Each of these steps is described in more detail in the following sections of this publication and summarized in the following flowchart.

Figure 1.1 – General framework for determining the accounting acquirer of a business





Grant Thornton insight: Reverse acquisition involving a VIE

Under ASC 805, the legal acquiree may be identified as the accounting acquirer in a business combination, in which case, the legal acquiree should apply purchase accounting to the legal acquirer. These transactions are known as “reverse acquisitions.”

After entities adopt the amendments in ASU 2025-03, transactions primarily effected by the exchange of equity interests where the legal acquiree is a VIE that meets the definition of a “business” may qualify as *reverse acquisitions*, as defined in ASC 805-40-30-2. Prior to the adoption of ASU 2025-03, such transactions would not have qualified as reverse acquisitions.



[This guidance applies prior to the adoption of the amendments in ASU 2025-03]

ASC 805-10-25-5

The guidance in the General Subsections of Subtopic 810-10 related to determining the existence of a controlling financial interest shall be used to identify the acquirer—the entity that obtains control of the acquiree. If a business combination has occurred but applying that guidance does not clearly indicate which of the combining entities is the acquirer, the factors in paragraphs 805-10-55-11 through 55-15 shall be considered in making that determination. 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 determination of which party, if any, is the primary beneficiary of a VIE shall be made in accordance with the guidance in the Variable Interest Entities Subsections of Subtopic 810-10, not by applying either the guidance in the General Subsections of that Subtopic, relating to a controlling financial interest, or in paragraphs 805-10-55-11 through 55-15.



[This guidance applies after adopting the amendments in ASU 2025-03]

ASC 805-10-25-5

The guidance in the General Subsections of Subtopic 810-10 related to determining the existence of a controlling financial interest shall be used to identify the acquirer—the entity that obtains control of the acquiree. If a business combination has occurred but applying that guidance does not clearly indicate which of the combining entities is the acquirer, the factors in paragraphs 805-10-55-11 through 55-15 shall be considered in making that determination. However, in a business combination in which a variable interest entity (VIE) is acquired, the primary beneficiary of that entity is the acquirer unless the business combination is effected primarily by exchanging equity interests. The determination of which party, if any, is the primary beneficiary of a VIE shall be made in accordance with the guidance in the Variable Interest Entities Subsections of Subtopic 810-10, not by applying either the guidance in the General Subsections of that Subtopic, relating to a controlling financial interest, or the guidance in paragraphs 805-10-55-11 through 55-15. For a business combination that is effected primarily by exchanging equity interests in which a VIE is acquired, the factors in paragraphs 805-10-55-12 through 55-15 shall be considered in determining which entity is the accounting acquirer.

2. Applying the guidance in ASC 810-10

Before identifying the acquirer, an entity must first assess whether the acquired entity qualifies as a VIE in accordance with the guidance provided in ASC 810, as discussed in Section 1.

If the acquired entity does not qualify as a VIE and is therefore considered a VOE, the subsequent step is to evaluate whether the guidance in ASC 810 clearly identifies which of the combining entities has obtained control over the others and is, therefore, the acquirer in the transaction.

2.1 Variable interest entity considerations

The primary beneficiary of a VIE is identified using the guidance in the VIE subsections of ASC 810-10. An entity applies the guidance in ASC 810-10-15-14 to determine whether the acquiree qualifies as a VIE. This evaluation can be complex and is outside the scope of this publication. Entities should look to the applicable guidance in making this determination.

While an acquired business might consist of an integrated set of assets and liabilities that meets the definition of a “business” in ASC 805, only a set that qualifies as a “legal entity” under ASC 810 is eligible to be considered a VIE.

Business: An integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing a return in the form of dividends, lower costs, or other economic benefits directly to investors or other owners, members, or participants.

Legal entity: Any legal structure used to conduct activities or to hold assets. Some examples of such structures are corporations, partnerships, limited liability companies, grantor trusts, and other trusts.

In general, if any one of the following three conditions outlined in ASC 810 exists, a legal entity is considered a VIE:

- The total equity investment at risk is not sufficient to permit the legal entity to finance its activities without additional subordinated financial support provided by any parties, including equity holders.
- As a group, the holders of the equity investment at risk lack the power, through voting rights or similar rights, to direct the activities of a legal entity that most significantly impact the entity’s economic performance, the obligation to absorb the expected losses of the legal entity, or the right to receive the expected residual returns of the legal entity.
- The equity investors as a group lack the power through voting or similar rights to direct the activities of the legal entity if:
 - The voting rights of some investors are not proportional to their rights to receive returns or their obligations to absorb losses of the legal entity, or both; or

- Substantially all of the legal entity's activities either involve or are conducted on behalf of an investor with disproportionately few voting rights.

Prior to the adoption of ASU 2025-03, the entity identified as the primary beneficiary of the VIE is deemed to be the accounting acquirer in a business combination involving the acquisition of a VIE.

Following the adoption of ASU 2025-03, an entity may no longer presume that the primary beneficiary of a VIE is the accounting acquirer in transactions primarily effected through the exchange of equity interests. In such cases, the determination of the accounting acquirer requires further evaluation using the factors in ASC 805-10-55-12 through 55-15.

When a reporting entity becomes the primary beneficiary of a VIE that is *not* considered to be a business under ASC 805, the primary beneficiary should initially measure and recognize the acquired assets and liabilities of the VIE in accordance with the acquisition method in ASC 805-20-25 and 805-20-30, except for goodwill, which is not recognized. Any assets or liabilities transferred by the primary beneficiary to the VIE in connection with becoming the VIE's primary beneficiary should be recognized at the amount at which the assets and liabilities would have been measured by the reporting entity had they not been transferred. Finally, the primary beneficiary of a VIE that is not a business should recognize a gain or loss upon becoming the primary beneficiary of the VIE as the difference between (a) the sum of the fair value of consideration paid, the fair value of any noncontrolling interests in the VIE, and the reported amount of any previously held interests in the VIE, and (b) the net amount of the VIE's identifiable assets and liabilities recognized and measured in accordance with ASC 805.

If the acquiree does not qualify as a VIE, the entity next evaluates whether the guidance in the general subsections of ASC 810 (that is, the VOE model) clearly identifies the accounting acquirer.

2.2 Voting interest entity considerations

Under the VOE model in ASC 810-10, ownership of 50 percent or more of the outstanding voting shares of an entity generally indicates that a controlling financial interest in that entity exists. However, there are other factors to consider that might influence an entity's ability to control another entity. For instance, control could also come in the form of a contractual agreement, a lease, an agreement with stockholders, or a decree from a court, even without ownership of 50 percent or more of the other entity's outstanding voting shares.

What's more, the evaluation of control in a limited partnership differs from the evaluation of control for a corporation or other similar entity. For limited partnerships managed by a general partner or other similar entities (such as limited liability companies that are managed by a managing member), kick-out rights that can be exercised without restriction by a simple majority (or less) of the limited partners' voting interests in the limited partnership are comparable to voting rights of shareholders in a corporation, and should be evaluated in determining a controlling financial interest. A limited partner that owns 50 percent or more of the limited partnership's kick-out rights through voting interests generally is considered to have a controlling financial interest in that partnership. Similar to corporations, other types of agreements and legal documents should be considered in the analysis to determine if a partner can exert control with even less than 50 percent of the kick-out rights.

If ASC 810 does not clearly identify the acquirer in a business combination, such as when a transaction is primarily effected by the exchange of equity interests, additional criteria are outlined in ASC 805 that should be used to make that determination, as discussed in Section 3.

**ASC 810-10-15-8**

For legal entities other than limited partnerships, the usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one reporting entity, directly or indirectly, of more than 50 percent of the outstanding voting shares of another entity is a condition pointing toward consolidation. The power to control may also exist with a lesser percentage of ownership, for example, by contract, lease, agreement with other stockholders, or by court decree.

ASC 810-10-15-8A

Given the purpose and design of limited partnerships, kick-out rights through voting interests are analogous to voting rights held by shareholders of a corporation. For limited partnerships, the usual condition for a controlling financial interest, as a general rule, is ownership by one limited partner, directly or indirectly, of more than 50 percent of the limited partnership's kick-out rights through voting interests. The power to control also may exist with a lesser percentage of ownership, for example, by contract, lease, agreement with partners, or by court decree.

3. Applying the guidance in ASC 805

For a VOE, if applying the guidance in ASC 810-10 does not clearly indicate which entity in a business combination is the acquirer, an entity must make that determination using the additional factors in ASC 805-10-55-11 to 55-15 (see table below).

If the acquired entity is a VIE and the transaction is effected primarily through the exchange of equity interests, an entity that has adopted the amendments in ASU 2025-03 would use the additional factors in ASC 805-10-55-12 to 55-15 to identify the accounting acquirer.

There is no hierarchy for considering these factors nor specified weighting, so judgment is required if using these criteria to identify the acquirer. All pertinent factors should be considered, and the amount of weight given to each one will vary based on the particular facts and circumstances of the transaction.



[Prior to adoption of ASU 2025-03]

ASC 805-10-55-10

Paragraph 805-10-25-5 provides that the guidance in the General Subsections of Subtopic 810-10 related to determining the existence of a controlling financial interest should be used to identify the acquirer in a business combination, except when a variable interest entity (VIE) is acquired. If a business combination has occurred but applying that guidance does not clearly indicate which of the combining entities is the acquirer, paragraph 805-10-25-5 requires the factors in paragraphs 805-10-55-11 through 55-15 to be considered in making that determination.

The additional indicators outlined in ASC 805-10-55-11 through 55-14 are summarized in the table below. Further discussion of each indicator is included in the rest of this section.

Indicator and ASC reference	Indications of which entity is the acquirer	Post ASU 2025-03: Applicable to a business combination with a VIE primarily effected by equity interests
The business combination is effected primarily by transferring cash or other assets or by incurring liabilities (ASC 805-10-55-11)	The entity that either transfers the cash or other assets or incurs the liabilities	N

Indicator and ASC reference	Indications of which entity is the acquirer	Post ASU 2025-03: Applicable to a business combination with a VIE primarily effected by equity interests
The business combination is effected primarily by exchanging equity interests (ASC 805-10-55-12)	The entity that issues its equity interests	Y
The relative voting rights in the combined entity after the business combination (ASC 805-10-55-12)	The entity whose owners have the largest voting rights in the combined entity	Y
The existence of a large minority voting interest in the combined entity if no single owner or organized group of owners has a significant voting interest (ASC 805-10-55-12)	The combining entity that has the largest minority voting interest	Y
The composition of the governing body of the combined entity (ASC 805-10-55-12)	The entity whose precombination ownership group can elect, appoint, or remove a majority of the combined entity's governing body	Y
The composition of senior management of the combined entity (ASC 805-10-55-12)	The entity whose precombination senior management team dominates the combined entity's senior management team	Y
The terms of the exchange of equity interests (ASC 805-10-55-12)	The entity that pays a premium exceeding the precombination fair value of the equity interests of the other combining entity or entities	Y
The relative size of the entities (ASC 805-10-55-13)	The precombination entity that is significantly larger than the other(s)	Y
The business combination involves more than two entities (ASC 805-10-55-14)	The entity that initiates the transaction	Y

3.1 Transferring cash, other assets, or incurring liabilities

According to ASC 805-10-55-11, if a business combination of a VOE is completed by transferring cash or other assets or by incurring liabilities, the acquirer is often the party that either transfers the cash or incurs the liabilities.



ASC 805-10-55-11

In a business combination effected primarily by transferring cash or other assets or by incurring liabilities, the acquirer usually is the entity that transfers the cash or other assets or incurs the liabilities.



Grant Thornton insight: Is ASC 805-10-55-11 determinative?

A question may arise as to whether an entity that effects a business combination of a VOE by transferring cash or other assets or by incurring liabilities must also consider the indicators listed in ASC 805-10-55-12 through 55-15 to identify the acquirer in a business combination. Some have questioned the relevance of these other indicators to transactions effected by cash, given that some of the indicators (for example, relative voting rights or the composition of the governing body) are only listed as subsections under ASC 805-10-55-12, which pertains only to business combinations effected primarily by exchanging equity interests.

ASC 805-10-55-10 specifies, in part, that “If a business combination has occurred but applying [the guidance in ASC 810] does not clearly indicate which of the combining entities is the acquirer, paragraph 805-10-25-5 requires the factors in paragraphs **805-10-55-11 through 55-15** to be considered in making that determination.” [emphasis added] As a result, we believe that entities evaluating business combinations with VOEs effected primarily by transferring cash or other assets or by incurring liabilities should consider the guidance in ASC 805-10-55-12 through 55-15 when identifying the acquirer in the transaction. In other words, in a business combination effected primarily by transferring cash or other assets or by incurring liabilities, we believe that the acquirer may not necessarily be the entity that transfers the cash or other assets or incurs the liabilities. However, we do believe that significant weight would be placed on ASC 805-10-55-11 for a business combination effected primarily by transferring cash or other assets.

3.2 Exchange of equity interests

If a business combination is completed through an exchange of equity interests, the entity issuing the equity interests, such as stock, is usually the acquirer. However, this is not the only consideration in identifying the acquirer in this situation. The guidance in ASC 805-10-55-12 also requires entities to consider the following indicators:

- Which entity has the most voting rights post-acquisition
- Which entity has a large minority voting interest in the combined entity, as long as no other owner has a significant voting interest
- Which entity has the most board seats in the combined entity

- Which entity's former management carries over to the combined entity
- Which entity pays a premium for the acquisition

Each of the indicators listed in ASC 805-10-55-12 are discussed in detail in this section.



ASC 805-10-55-12

In a business combination effected primarily by exchanging equity interests, the acquirer usually is the entity that issues its equity interests. However, in some business combinations, commonly called reverse acquisitions, the issuing entity is the acquiree. Subtopic 805-40 provides guidance on accounting for reverse acquisitions. Other pertinent facts and circumstances also shall be considered in identifying the acquirer in a business combination effected by exchanging equity interests, including the following:

- a. The relative voting rights in the combined entity after the business combination. The acquirer usually is the combining entity whose owners as a group retain or receive the largest portion of the voting rights in the combined entity. In determining which group of owners retains or receives the largest portion of the voting rights, an entity shall consider the existence of any unusual or special voting arrangements and options, warrants, or convertible securities.
- b. The existence of a large minority voting interest in the combined entity if no other owner or organized group of owners has a significant voting interest. The acquirer usually is the combining entity whose single owner or organized group of owners holds the largest minority voting interest in the combined entity.
- c. The composition of the governing body of the combined entity. The acquirer usually is the combining entity whose owners have the ability to elect or appoint or to remove a majority of the members of the governing body of the combined entity.
- d. The composition of the senior management of the combined entity. The acquirer usually is the combining entity whose former management dominates the management of the combined entity.
- e. The terms of the exchange of equity interests. The acquirer usually is the combining entity that pays a premium over the precombination fair value of the equity interests of the other combining entity or entities.

In a *reverse acquisition* or a *reverse merger*, the entity issuing its shares is identified as the acquiree instead of as the acquirer.

3.2.1 Relative voting rights

The relative voting rights held by the precombination shareholder groups of the combining entities in the combined entity after the business combination is a factor that must be evaluated to see which entity's owners, as a group, retain or receive the largest portion of voting rights in the combined entity and may therefore be the acquirer.

The guidance in ASC 805 specifies that an entity should consider all of the following instruments or arrangements when evaluating the relative voting rights:

- Options, warrants, and convertible securities

- Other unusual or special voting arrangements



Grant Thornton insight: Considerations for options, warrants, and convertible securities

When considering the impact of equity-linked instruments that do not vote, but could convey potential voting rights to the precombination shareholder groups, entities should consider in-the-money options, warrants, and convertible securities that are vested and exercisable or are convertible into voting interests as of the acquisition date when analyzing the relative voting rights in the combined entity. Further, all warrants (or other similar contracts in an entity's equity) that allow holders to vote prior to exercising the warrant should also be considered in the analysis.

When determining relative voting rights, an entity generally would not consider certain other instruments, such as out-of-the-money instruments that can be exercised or converted at the acquisition date or instruments that do not vest or cannot be exercised or converted until after the acquisition; however, certain facts and circumstances, as described in the following table, may require entities to exercise judgment when considering whether these instruments could impact the analysis.

Types of instruments	Factored into relative voting right analysis?
All securities with voting rights	Yes
Special voting arrangements	Yes
Vested and in-the-money options or warrants, as well as vested and exercisable convertible securities that can be converted as of the acquisition date	Yes
Vested and out-of-the-money options or warrants, as well as vested and exercisable convertible securities that can be converted as of the acquisition date	Use judgment considering, among other factors, the extent to which the instruments are out-of-the-money, their volatility, and the length of the exercise period



Grant Thornton insight: Weighting of voting rights

While ASC 805 does not explicitly prescribe how to weight the indicators in ASC 805-10-55-12, a generally accepted practice is to give increasing weight to the "relative voting rights" indicator as the relative percentage of voting rights held by the precombination shareholder groups of the combining entities deviates from a 50-50 ownership. In other words, if Entity A and Entity B enter into a business combination by exchanging equity interests and, after the combination, Entity A's precombination shareholders hold 51 percent of the voting rights in the combined entity while Entity B's precombination shareholders hold 49 percent, this "relative voting rights" indicator, in practice, is given less weight than

when Entity A's precombination shareholders hold 75 percent of the voting rights while Entity B's precombination shareholders hold 25 percent.

3.2.2 Large minority voting interest

In some business combinations, especially those involving multiple entities, one single precombination owner of one of the combining entities may not gain a majority voting interest in the combined entity. Instead, there may be multiple precombination owners of the combining entities with minority interests in the combined entity. In this case, the precombination owner or group of owners that holds the largest minority interest in the combined entity may be the acquirer.



Large minority voting interest

Entity A and Entity B, both businesses, merge. Entity A's and Entity B's former shareholders each collectively own approximately 50 percent of the voting interest of the combined entity; however, no single precombination investor in either Entity A or Entity B owns more than 3 percent of the outstanding voting shares of the combined entity, with one exception: a former shareholder of Entity B owns 35 percent of the outstanding voting shares of the combined entity. As a result, the large minority interest (relative to other minority interests) within the precombination ownership group of Entity B is an indicator that points to Entity B as the accounting acquirer.

3.2.3 Composition of the governing board of combining entity

If a combined entity following a business combination is controlled by a board of directors, the acquirer may be the entity whose precombination ownership group has the right to elect, appoint, or remove a majority of the members of the board of the combined entity.



Grant Thornton insight: Considering the composition of the combined entity's governing board

At the 2007 AICPA National Conference on Current SEC and PCAOB Developments, the SEC staff's Eric West [indicated](#) that the goal of evaluating the composition of the combined entity's governing board is to determine whether any precombination shareholder group has substantive control of the combined entity's board. According to Mr. West, this evaluation may require consideration of how long each board member is entitled to serve on the board and whether a board member represents the majority or minority shareholders of the combined entity. An important step in this evaluation is to determine whether control of the board by any precombination shareholder group is temporary, in which case, control may not be substantive.

This step is particularly important in situations where the board of directors of the combined entity is dominated by members that represent the minority shareholders' interests. If a precombination shareholder group's control of the board is only temporary, then control may not be considered substantive. However, Mr. West emphasized that the evaluation of whether control of the board is

substantive requires judgment, and the SEC staff has not established a bright line for determining whether temporary control by board members constitutes substantive control.

In light of this speech, we believe that the following considerations, among others, will assist entities when determining which shareholder group of the combining entity has substantive control of the board, which could indicate that it is the accounting acquirer:

- What are standard terms for board members and are there any exceptions to those terms?
- How are board members appointed and replaced?
- Who makes appointments and controls the vote to replace board members?
- What operational decisions does the board have voting rights over?
- How are matters approved, by a simple majority or otherwise?
- If there is a tie vote, what is the process for resolving that tie?

3.2.4 Composition of senior management

According to ASC 805, the acquirer is usually identified as the combining entity whose former management makes up the majority of, or holds the key positions in, the senior management roles of the combined entity. In practice, the roles that constitute senior management include the chief executive officer, the chief operating officer, the chief financial officer, and any other executive committee members. Postcombination entities should also consider the duration of senior management's employment contracts when evaluating this indicator.



Grant Thornton insight: Composition of senior management

When the composition of a combined entity's senior management is split evenly between the former management of the pre-acquisition entities, the combined entity should generally look to key positions that are most critical to the combined entity's business. When one of the combining entities' former management holds the key positions in the postcombination entity, that would indicate that this entity is the accounting acquirer.

Determining which roles in the postcombination entity comprise the key positions may require judgment. For example, if two businesses combine to form an electric car manufacturer, the senior management positions deemed to be most critical to the combined entity's success might include those related to the design and manufacture of the vehicles, such as the chief engineer and chief technology officer (or similar roles).

Alternatively, if two businesses combine to form a pharmaceutical company, the senior management positions deemed to be most critical to the combined entity's success might include those related to the development of new drug candidates, such as the chief medical officer and chief R&D officer (or similar roles).

3.2.5 Terms of the exchange of equity interests

The combining entity that pays a premium over the precombination fair value of the equity interests of the other combining entity (or entities) is usually identified as the acquirer in a business combination transaction.



Grant Thornton insight: Terms of the exchange of equity interests

A combining entity that pays a premium over the precombination fair value of the equity interests of the other combining entity (or entities) is a relevant indicator of the accounting acquirer only to the extent that the fair value is objectively determinable, which would be case only if the precombination entities are publicly traded companies. In reality, when the combining entities are not public business entities, it might be challenging to determine whether one of the combining entities pays a premium over the precombination fair value of the equity interest of the other combining entity (or entities), since the fair value of the equity instruments is less objectively determinable.

3.2.6 Relative size

A combining entity that is significantly larger than the other combining entity (or entities) might indicate that the significantly larger entity is the accounting acquirer. The size of the entities could be measured based on assets, revenues, earnings, or other relevant benchmarks.



ASC 805-10-55-13

The acquirer usually is the combining entity whose relative size (measured in, for example, assets, revenues, or earnings) is significantly larger than that of the other combining entity or entities.



Grant Thornton insight: Considering relative size

When determining which of the combining entities is the accounting acquirer, considering the relative sizes of the precombination entities is generally straightforward for entities in the same line of business. However, when entities from different industries combine, this evaluation may require significant judgment to find a meaningful operating metric to use for comparing their relative sizes, if one exists at all. Furthermore, entities in the same line of business may even need to adjust their analysis to determine the relative size (for example, for different accounting policies).

3.3 Business combinations involving more than two entities

Only one acquirer may be identified in a business combination. ASC 805 explicitly states that entities should apply the acquisition method to combinations involving more than two entities (often referred to as “roll-up” or “put-together” transactions), combinations between two or more mutual entities, and true mergers of equals, even though one entity might not “obtain control” over another in some of these situations. Specifically, when determining which of the combining entities is the acquirer in combinations

involving more than two entities, ASC 805 requires entities to consider which one of the combining entities initiated the transaction as well as the relative sizes of the combining entities.



ASC 805-10-55-14

In a business combination involving more than two entities, determining the acquirer shall include a consideration of, among other things, which of the combining entities initiated the combination, as well as the relative size of the combining entities

3.4 Newco considerations

One strategy many entities use to facilitate a business combination is the creation of a new entity (often referred to as “Newco”) that then carries out the business combination. Only a substantive Newco may be considered the accounting acquirer. ASC 805-10-55-15 says that a Newco formed only to issue equity interests to effect a business combination is not considered to be substantive and therefore cannot be identified as the accounting acquirer.

Therefore, in business combinations involving a Newco, entities should first consider whether Newco is substantive and, if so, should analyze Newco along with the other combining entities using the applicable guidance in ASC 805-10-55-10 through 55-14 to identify the accounting acquirer.



ASC 805-10-55-15

A new entity formed to effect a business combination is not necessarily the acquirer. If a new entity is formed to issue equity interests to effect a business combination, one of the combining entities that existed before the business combination shall be identified as the acquirer by applying the guidance in paragraphs 805-10-55-10 through 55-14. In contrast, a new entity that transfers cash or other assets or incurs liabilities as consideration may be the acquirer.



Grant Thornton insight: Considering the definition of a ‘business’ when evaluating Newcos

Newcos generally do not meet the definition of a “business” in ASC 805. However, ASC 805 defines a “business combination” as “A transaction or other event in which an acquirer obtains control of one or more businesses.”

Accordingly, while the acquirer does not need to constitute a “business,” as defined in ASC 805-10-55-3A through 55-6 and in 55-8 to 55-9, for the transaction to constitute a business combination, the acquiree must qualify as a business. When evaluating combinations between entities involving Newcos, it is important to keep in mind that the Newco need not constitute a business to be identified as the accounting acquirer, but one of the other combining entities must constitute a business, as defined.

3.4.1 Determining if Newco is substantive

In practice, the following questions are used to determine if a Newco is substantive. None of the factors alone is determinative, and the guidance does not prescribe weighting. Entities must consider all facts and circumstances when analyzing these transactions as they often require significant judgment.

Questions to consider whether Newco is substantive	Analysis
Does Newco have a change in control when considering the equity holders of Newco compared to those of the target company prior to the merger?	A change in control when considering the composition of equity holders of Newco and the equity holders of the target prior to the merger may serve as an indicator that Newco is substantive.
Does Newco have significant precombination activities, such as raising capital, identifying and promoting acquisition targets, and negotiating transactions, among other practices?	Significant precombination activities suggest Newco is substantive, while no or insignificant precombination activities indicate that Newco was formed purely to effect the transaction and therefore may indicate Newco is nonsubstantive.
Does Newco survive the transaction?	A Newco that is transitory or does not survive the transaction might indicate that Newco lacks substance and therefore might not be considered the acquirer. A Newco that is not transitory and survives the transaction might indicate that Newco has substance.
Does Newco pay cash or other assets, or incur debt to effect the transaction?	As stated in ASC 805-10-55-15, a Newco that issues equity interest only to effect a business combination lacks substance and cannot be considered an acquirer. However, a Newco that pays cash or other assets or incurs debt may suggest that Newco is substantive and therefore may be considered the acquirer.
How does the composition of the board of directors of Newco compare to that of the target?	A board of directors of Newco that consists primarily of the same board members from one or more of the other precombination entities indicates that Newco may not be substantive.
How does the composition of the senior management of Newco compare to that of the target?	Senior management of Newco that consists primarily of the same team that was in place at one or more of the other precombination entities may indicate that Newco is not substantive.



Evaluating whether Newco is substantive

Scenario 1

Entity A and Entity B agree to combine in a transaction that is a business combination. Newco is formed to effect the business combination and issue common shares to the shareholders of both Entity A and Entity B. When the transaction is complete, Entity A and Entity B are each wholly owned subsidiaries of Newco.

Newco is not substantive and therefore cannot be the accounting acquirer. While Newco is not transitory and survives the transaction, as discussed in ASC 805-10-55-15, if a new entity is formed to issue equity interests to effect the business combination, one of the combining entities that existed before the business combination (either Entity A or Entity B) should be identified as the acquirer under the guidance in ASC 805-10-55-10 through 55-14. The transaction is not substantively different than a transaction in which one of the combining entities directly acquires the other.

Scenario 2

Entity A and Entity B agree to combine in a transaction that is a business combination. Newco will be formed the moment the business combination closes to effect the transaction. Newco will be transitory. Newco does not have any significant precombination activities, and its board of directors and senior management are dominated by individuals from Entity A.

In this situation, Newco is not substantive. Newco does not survive the transaction and does not have any significant precombination activities. In addition, the fact that Newco's board of directors and senior management is dominated by Entity A suggests that Newco lacks substance.

Scenario 3

Entity A forms Newco to facilitate a merger between Entity A and Entity B. Newco is formed six months prior to the business combination and survives the transaction. Newco raises debt in its own name to fund the acquisition. Newco's board of directors and senior management are predominantly comprised of individuals who were not previously affiliated with Entity A nor Entity B.

In this situation, Newco is substantive and can be identified as the accounting acquirer. Not only does Newco survive the transaction, but it has significant precombination activities and raises debt in exchange for its interest in the target. Further, the governance structure of Newco is predominantly different from that of Entity A or Entity B.

3.4.2 Evaluating if a substantive Newco is the acquirer

Although a Newco that is considered substantive is eligible to be the acquirer, an entity may still need to consider the guidance in ASC 805-10-55-10 through 55-14 to determine which of the combining entities should be identified as the acquirer.



Determining whether substantive Newco is the acquirer

Entity A forms Newco to facilitate a merger between Entity A and Entity B. Newco is formed six months prior to the business combination and survives the transaction. Newco raises debt in its own name to fund the acquisition of 51 percent of Entity A. Newco's board of directors and senior management are predominantly comprised of individuals from Entity A. Owners from Entity A will own 51 percent of the voting rights of Newco after the transaction, while new investors will own 49 percent of the voting rights. Entity A is significantly larger than Newco in terms of assets and revenues.

In this situation, Newco is substantive and may be identified as the accounting acquirer. Not only does Newco survive the transaction, but it has significant precombination activities and raises debt and uses the proceeds to purchase its interest in the target. However, upon review of the indicators in ASC 805-10-55-12 through 55-14, management determines that Entity A is the acquirer because Newco's board of directors and senior management are predominantly comprised of individuals from Entity A, Entity A's precombination owners will own 51 percent of the voting rights of Newco after the transaction, and due to Entity A's size relative to Newco's size.

Appendix A

Titles in FASB Accounting Standards Codification (ASC)

ASC 805	<i>Business Combinations</i>
ASC 805-10	<i>Business Combinations: Overall</i>
ASC 805-20	<i>Business Combinations: Identifiable Assets and Liabilities, and Any Noncontrolling Interest</i>
ASC 805-50	<i>Business Combination: Related Interests</i>
ASC 810	<i>Consolidation</i>
ASC 810-10	<i>Consolidation: Overall</i>

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