

Audit Alert: FASB clarifies the definition of a “business”

The Board issued ASU 2017-01, [*Clarifying the Definition of a Business*](#), which provides a new framework for entities to use when determining whether a set of assets and activities (together referred to as “a set”) constitutes a business. The amendments in the ASU will assist entities when they evaluate whether transactions should be accounted for as acquisitions (or disposals) either of assets or of businesses. This distinction is important since there are significant differences between the accounting for an acquisition of a business and for an acquisition of assets.

Under ASC 805, *Business Combinations*, an entity determines whether a transaction is a business combination based on whether the acquired activities and assets meet the definition of a business. If these acquired activities and assets constitute a business, an entity would then use the acquisition method to account for the assets acquired and liabilities assumed in the transaction. As a result, the definition of a business directly impacts the accounting for acquisitions along with many other areas of accounting, including disposals, goodwill, and consolidation.

As an initial step in determining whether a set is a business, the amendments provide a screen to determine when a set is not a business. When applying the screen, if substantially all of the fair value of the gross assets acquired is concentrated in a single identifiable asset or in a group of similar

identifiable assets, the set is not a business, and no further assessment is required. This screen is expected to reduce the number of transactions that would require further evaluation.

The amendments also include additional guidance related to applying the screen, and the steps to perform if the screen is not met and it also removes the evaluation of whether a market participant can replace any missing elements. Additionally, the definition of an output has been amended so that this term is consistent with the description of outputs in ASC 606, *Revenue from Contracts with Customers*.

The amendments are effective for public business entities, in annual periods beginning after December 15, 2017 and all other entities in annual periods beginning after December 15, 2018.

These amendments should be applied prospectively on or after the effective date.

Source: Grant Thornton, On the Horizon, January 12, 2017

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