

FINANCIAL STATEMENTS OF ACQUIRED BUSINESSES: A SNAPSHOT

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This guide provides a high-level summary of the SEC's financial statement requirements for significant business acquisitions.

WHERE TO START:

When evaluating the financial reporting ramifications for an acquisition, companies should begin by answering the two following questions:

- ▶ Is the company acquiring a “business,” as defined by Regulation S-X?
- ▶ What is the significance of the acquired business to the registrant?

The answers to these questions will ultimately drive the financial statements to be filed in Form 8-K and any subsequently filed registration statements.

IS THE ACQUISITION A “BUSINESS”

Regulation S-X Rule 11-01(d)

There is a presumption that a legal entity, subsidiary, or a division is a business, though a lesser component of an entity may also constitute a business and will generally depend on whether the nature of the revenue-producing activity is the same before and after the acquisition (among other factors).

IS THE ACQUIRED BUSINESS “SIGNIFICANT”

Regulation S-X Rules 3-05 and 1-02(w)

The significance of an acquired business (“target”) to the registrant (“acquiror”) is based on three tests, and the highest percentage of the three tests is used to determine the financial reporting requirements.

Asset Test	Target's total assets compared to acquiror's total assets as of the end of the most recently completed fiscal year
Investment Test	Fair value of the acquiror's investment in the target (i.e., GAAP purchase price) compared to acquiror's average aggregate worldwide market value
Income Test	LOWER OF: Target's pre-tax income from continuing operations attributable to controlling interests compared to acquiror's pre-tax income from continuing operations attributable to controlling interests for most recently completed fiscal year -OR- Target's total revenue compared to acquiror's revenue for most recently completed fiscal year

Additionally, a registrant is permitted to use pro forma financial information to measure significance for acquisitions completed after the latest fiscal year end if the registrant has filed:

- ▶ The required target financial statements, and
- ▶ The required Article 11 pro forma financial information for any such acquired business.

WHEN TO REPORT A SIGNIFICANT ACQUIRED BUSINESS:

	STEP 1	STEP 2	STEP 3
Action	Sign the Purchase Agreement	Close the Acquisition	File the Required Financial Statements
When & what to file	Within 4 business days, File Item 1.01 Form 8-K	Within 4 business days, file Item 2.01 Form 8-K	Within 71 calendar days after Step 2, file Item 9.01 Form 8-K

If the acquired business financial statements are required in connection with a registration statement (as summarized below), they may be included in the registration statement or incorporated by reference from a Form 8-K filing.

FINANCIAL STATEMENTS OF AN ACQUIRED BUSINESS IN FORM 8-K:

The historical financial statement requirements for the target to be filed in Form 8-K are based on bright-line significance thresholds set forth in S-X Rule 3-05 as follows:

SIGNIFICANCE	REQUIRED TARGET FINANCIAL STATEMENTS
20% or less	No financial statements
More than 20% but not more than 40%	One year of audited financial statements and unaudited interim financial statements for the current year (no prior year interims required)
More than 40%	Two years of audited financial statements and comparative current and prior year unaudited interim financial statements

The age of the target's financial statements depends on whether the target is private or public (and if public, the filing status of the target). For example, the age of a privately held target's financial statements to be included in Form 8-K is based on the following:

Age is determined by reference to:	The earlier of the filing date or due date of Step 2 Form 8-K
Annual financial statements	Required when Step 2 Form 8-K is due 90 days or more after target's fiscal year end
Interim financial statements	Latest balance sheet must be within 135 days of the Step 2 Form 8-K due date, except that the 3rd quarter is considered timely through the 90th day after the target's fiscal year end

FINANCIAL STATEMENTS OF AN ACQUIRED BUSINESS IN A REGISTRATION STATEMENT:

SIGNIFICANCE	REQUIRED TARGET FINANCIAL STATEMENTS
20% or less	No financial statements
More than 20% but not more than 40%	If the target has been included in the audited financial statements of the registrant for a period of 9 months, no financial statements are needed. Otherwise, continue to present one year of historical audited financial statements and unaudited interim financial statements for the current year (no prior year interims required).
More than 40%	If the target has been included in the audited financial statements of the registrant for a complete fiscal year (i.e., twelve months), no financial statements are needed. Otherwise, continue to present two years of historical audited financial statements and comparative current and prior year unaudited interim financial statements.

Registrants also need to consider the aggregate effect of all business acquisitions that have been completed or are probable since the date of the most recent audited balance sheet filed for the registrant. If the aggregate effect of such acquisitions exceeds 50% significance for the asset, investment or income tests, registrants are required to file:

- ▶ Pre-acquisition historical audited financial statements for any target whose individual significance exceeds 20%; and
- ▶ Pro forma financial information depicting the aggregate effects of all such "individually insignificant businesses" in all material respects.

The ages of the annual and interim financial statements for a privately-held target in a registration statement are as follows:

Age is determined by reference to:	The effective date of the registration statement
Annual financial statements	Required when filing is effective after 89th day after target's fiscal year end -OR- May be required if filing is effective after 45 days but not more than 89 days after target's fiscal year end depending on the registrant's eligibility for relief under S-X Rule 3-01(c)
Interim financial statements	Latest balance sheet must be within 135 days of the effective date

PRO FORMA FINANCIAL INFORMATION

Regulation S-X Article 11

When a target's historical financial statements are required to be presented, pro forma financial information must also be presented that includes:

- ▶ A pro forma condensed balance sheet as of the end of the most recent period for which a balance sheet is required;
- ▶ Pro forma condensed statements of income from continuing operations for the last completed fiscal year and year-to-date interim period; and
- ▶ Accompanying explanatory notes.

Pro forma adjustments are required to give effect to the accounting for the acquisition. Additional management adjustments to reflect synergies and dis-synergies of the acquisition are optional and may be presented in the explanatory notes.



COMPANION PUBLICATIONS

Additional information on the SEC's pro forma financial information requirements for significant business acquisitions, and historical financial statement requirements for significant real estate operations can be found in our companion publications.

[Pro Forma Financial Information: A Snapshot](#)

[Financial Statements of Acquired Real Estate Operations: A Snapshot](#)

Contacts

TIM KVIZ

National Managing Partner, SEC Services
703-245-8685 / tkviz@bdo.com

PAULA HAMRIC

Professional Practice Partner, SEC Services
312-616-3947 / phamric@bdo.com

BRANDON LANDAS

Professional Practice Partner, SEC Services
312-233-1887 / blandas@bdo.com

SHERI FABIAN

Professional Practice Partner, SEC Services
732-734-3063 / sfabian@bdo.com

MEGHAN DEPP

Professional Practice Partner, SEC Services
248-688-3368 / mdepp@bdo.com

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