Real Externalities of Fair Value Estimates of Technology-related Intangibles: Evidence from Business Combinations

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Abstract

This study evaluates the decision-usefulness of audited fair value estimates for technology-related intangibles. Using SFAS 141-mandated Purchase Price Allocation (PPA) disclosures, we analyze how these estimates shape innovation strategies among firms with existing technological links to the acquisition target (TLFs). We find that TLFs increase their technological closeness to the target's pre-acquisition technology areas to a greater extent when the acquirer allocates a larger share of the total purchase price to the target's developed technology. This is consistent with TLFs using PPA disclosures to assess the relative profit potential of different technology areas and reallocate their innovation efforts accordingly. This relationship strengthens when the TLFs are more likely to attend to and respond to the acquirer's PPA disclosures. Furthermore, increased technological closeness to the target is associated with improved innovation outcomes for the TLFs, especially when the target's developed technology is assigned a higher fair value. Collectively, our findings suggest that fair value estimates can provide decision-useful information that influences the TLFs' resource allocation across technology areas, despite concerns about their reliability.

Keywords: Fair value estimates; Technology; Patent; Externality; Business combinations

JEL Classifications: D62, E22, M41, O31, O32, O33