FASB FINANCIAL ACCOUNTING STANDARDS BOARD

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Memo

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Project	**Accounting for Goodwill for Public Business Entities and Not-for-Profit Entities**
Project Stage	**Initial Deliberations**
Issue(s)	**Potential Model for Subsequent Measurement of Goodwill for Public Business Entities and Not-for-Profits**

Purpose of This Memo

1. The purpose of this memo is to provide a summary to the Boards of the progress to date by the FASB staff on the subsequent measurement of goodwill for public business entities and not-for-profits project. The project is currently in the initial deliberations stage.

2. On November 25, 2013, the FASB added this project to the technical agenda and asked the staff to analyze potential alternatives for the subsequent measurement of goodwill for public business entities (PBEs) and not-for-profit entities (NFPs). The project was added to the FASB's agenda at the same meeting the FASB endorsed the Private Company Council (PCC) recommendation for private companies for the subsequent measurement of goodwill.

3. This memo is organized as follows:

   (a) Summary of the FASB's past projects on the subsequent measurement of goodwill

   (b) Summary of current outreach activities and research

(c) Staff analysis and options

    (1) View A: PCC model

    (2) View B: Amortize goodwill

    (3) View C: Direct write-off

    (4) View D: Simplified impairment test

(d) Alternative or requirement for public business entities.

Summary of the FASB's Past Projects on the Subsequent Measurement of Goodwill

4. The FASB has considered and changed the accounting for the subsequent measurement of goodwill multiple times in recent years. Prior to 2002, all companies following generally accepted accounting principles (GAAP) amortized goodwill over its useful life, not to exceed 40 years, based on the requirements of Accounting Principles Board (APB) Opinion No. 17, *Intangible Assets*. In the 1999 Exposure Draft on business combinations and intangible assets (the 1999 Exposure Draft), the FASB proposed a reduction in the maximum life of goodwill from 40 years to 20 years as a part of a complete overhaul of accounting for business combinations, goodwill, and intangible assets. In the 1999 Exposure Draft, the FASB concluded that the life of goodwill cannot be predicted with a satisfactory level of reliability and the pattern in which goodwill diminishes cannot be known. Thus, amortization over an arbitrary period was the only practical solution.

5. Some respondents supported this amortization model. However, others challenged the use of an amortization model and/or the use of an arbitrary maximum period for amortization. The FASB ultimately agreed with those other respondents that "…straight-line amortization of goodwill over an arbitrary period does not reflect economic reality and thus does not provide useful information…" (paragraph B79 of FASB Statement No. 142, *Goodwill and Other Intangible Assets*).

6. In response to the feedback received, the FASB then developed a model that required an annual impairment test and did not permit amortization. The model was finalized in 2001 as part of Statement 142. While many stakeholders supported the concept of an impairment

model, feedback on the impairment model was mixed on whether it would work in practice and whether the previous proposal or another method for accounting for goodwill (such as a direct write-off of goodwill) was more appropriate.

7. The requirements of Statement 142 (and FASB Statement No. 141, *Business Combinations*) were deferred for NFPs. The accounting for mergers and acquisitions of NFPs was addressed separately as a part of FASB Statement No. 164, *Not-for-Profit Entities: Mergers and Acquisitions* (2009). Statement 164 requires NFPs that rely predominantly on contributions to write off goodwill at the acquisition date. Other more "business-like" entities (such as health care entities) account for goodwill in accordance with Statement 142. In addition, the combination of two NFPs can qualify as a merger under certain circumstances and the carryover basis of accounting would be applied (that is, no goodwill would be recognized). The acquisition guidance in Statement 164 was effective in 2010 for calendar-year entities (and effective for fiscal years ended June 30, 2011, for many NFPs).

8. In FASB Accounting Standards Update No. 2010-28, *Intangibles—Goodwill and Other (Topic 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts*, the Emerging Issues Task Force (EITF) concluded that if the carrying value of a reporting unit was zero or negative, certain factors should be used to determine if it is more likely than not that goodwill is impaired and if so, step 2 must be performed. These factors include, for example, consideration of declines in actual or planned revenue or earnings compared with relevant prior periods, changes in customers, a deterioration in the environment in which the entity operates, and increases in costs that have a negative effect on earnings and cash flows. Before this guidance, some entities always concluded that because the fair value of the reporting unit was higher than the carrying value (that was zero or negative), step 1 was passed over (and, thus, goodwill was not impaired).

9. In 2011, due to concerns about the cost and complexity of the annual goodwill impairment test, the FASB developed an optional qualitative impairment test as a screen for companies to assess whether it is more likely than not that goodwill is impaired before performing the quantitative impairment test (originally in the amendments in FASB Accounting Standards Update No. 2011-08, *Intangibles—Goodwill and Other (Topic 350): Testing Goodwill for Impairment;* now included in Subtopic 350-20, Intangibles—Goodwill and Other—

Goodwill). As part of the deliberations on that project, the FASB considered goodwill amortization and a direct write-off of goodwill. In the basis for conclusions in Update 2011-08, the FASB reaffirmed the decisions reached in connection with Statement 142 that (a) amortization was not appropriate because the pattern of expense recognition for goodwill often does not align with the economics of the goodwill recognized because not all goodwill declines in value and it is difficult to estimate a useful life and an appropriate pattern of amortization for any portion of goodwill that is wasting (paragraph BC15 of Update 2011-08) and (b) direct write-off is not appropriate because goodwill meets the definition of an asset; thus, goodwill should not be written off unless it is deemed impaired (paragraph BC16 of Update 2011-08).

10. In 2013, the PCC developed an alternative (described further below) that was endorsed by the FASB and included in FASB Accounting Standards Update No. 2014-02, *Intangibles—Goodwill and Other (Topic 350): Accounting for Goodwill*, permitting private companies to elect to amortize goodwill and perform a simplified impairment test on the occurrence of a triggering event. This alternative was based on feedback from private company stakeholders that the benefits of the subsequent measurement of goodwill prior to the alternative did not justify the costs for private companies. Users indicated that the existing goodwill impairment test provided limited decision-useful information, and preparers and auditors of private company financial statements indicated concerns over the cost and complexity involved in performing the impairment test.

11. The staff also notes that as a result of the recent PCC alternative related to the recognition of intangible assets in a business combination, the FASB is considering changes for PBEs and NFPs (see Memo 2). If other assets presently included in identifiable intangible assets are instead included in goodwill, the FASB's (and staff's) view about the subsequent measurement of goodwill may be significantly affected.

Summary of Current Outreach Activities and Research

Outreach and Research

12. For PBEs and NFPs, the staff performed the following outreach:

(a) Reviewed relevant comment letter responses and bases for conclusions from previous projects on the subsequent measurement of goodwill

(b) Performed outreach with PBE and NFP stakeholders, including preparers, users, the Investor Advisory Committee (IAC), large accounting firms, the Small Business Advisory Committee (SBAC), the Not-for-Profit Advisory Committee (NAC), and the American Institute of Certified Public Accountants' (AICPA) Not-for-Profit Entities Expert Panel.

13. The outreach activities conducted by the FASB staff indicated that some preparers struggle with the cost and complexity of the annual goodwill impairment test. Some assert that the qualitative test added in 2011 has not reduced cost or complexity. Financial Executives International (FEI) and Duff & Phelps have conducted studies focusing on the goodwill impairment test and the qualitative screen introduced in 2011, with the following results:

(a) Less than 30 percent of public company respondents to a 2013 FEI survey used the qualitative screen in 2012:

(1) Approximately 26 percent of the public company respondents to an FEI survey in 2013[1] considered using the screen, but did not because they felt the guidance was not practical or did not believe the test was cost effective.

(2) Approximately 45 percent of the public company respondents said that they did not use the screen because they preferred the quantitative test.

(b) A 2014 Duff & Phelps study expanded on the FEI surveys completed in past years by evaluating the disclosures for a selection of 355 public companies with goodwill to assess whether those companies use the qualitative screen, concluding:[2]

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[1] Duff & Phelps is a global valuation and corporate finance advisor. During the last six years, Duff & Phelps performed a goodwill impairment study in conjunction with the Financial Executives Research Foundation, which features a survey of the members of Financial Executives International about their qualitative goodwill impairment test usage. Click here for the 2013 study: Duff & Phelps, 2013 U.S. Goodwill Impairment Study, November 2013.

[2] Click here for the 2014 study: Duff & Phelps, Goodwill Impairment Step 0 Study, September 2014.

(1) Thirty-three percent of the sample public companies were either definite or probable users of the qualitative screen in 2012 [2] (which is consistent with the finding in the FEI study in the previous year).

(2) Definite or probable users from the same sample of public companies increased to 41 percent in 2013.

(3) The qualitative screen may be used more frequently than indicated by the results, because the disclosure requirements for goodwill impairment do not explicitly require an assertion about the use of the qualitative screen (which was the FASB's intent based on paragraph BC24 of Update 2011-08).

14. Many comment letter respondents to the PCC proposal, as well as others included in the staff's outreach (including users), believe that the subsequent measurement of goodwill is not an area that warrants a difference between public and private companies.

15. However, preparers were split on whether they prefer the current model for the subsequent measurement of goodwill versus another model (such as amortization or a direct write-off). Some of those that favor goodwill amortization were supportive primarily because they believe it would reduce cost and complexity, not because they thought it would provide better information to financial statement users. Concerns expressed by preparers about the PCC alternative (or amortization in general) included:

(a) Whether there is a strong conceptual basis for moving to an amortization model and testing goodwill at the entity level

(b) Whether the amortization period included in the PCC alternative is too short compared with the cash flows projected from an acquisition

(c) Whether any arbitrary maximum life for goodwill is appropriate

(d) How analysts and investors may perceive the "drag" on earnings from goodwill amortization.

(e) Some preparers believe goodwill amortization would be ignored.

16. All users of PBE financial statements that the staff spoke to said goodwill amortization would not provide relevant information and indicated that they would make an adjustment to

earnings for goodwill amortization. The staff observes from its research that users ignored goodwill amortization when goodwill was amortized prior to Statement 142.

17. While some users were indifferent to which model is used for the subsequent measurement of goodwill (more often lenders), many users (more often credit rating agencies and equity analysts) noted the following:

    (a) Impairment charges do provide some relevant information from a qualitative perspective.

    (b) Impairment charges are a lagging indicator of issues and are often anticipated (particularly if the issues that drive the impairment are industry-wide issues).

    (c) The exact amount of the impairment may not be important and is not directly used in projecting cash flows, but the general magnitude of impairment, frequency of impairment, and acknowledgement by management that future cash flows might be lower than anticipated can provide useful information.

    (d) The accumulation of impairment charges over time can inform an investor's view of management's business acumen and future prospects of the company.

    (e) Goodwill impairment is an area where users can gain insights into changes in management's cash flow projections.

18. Some users stated that they focus on tangible book value (or their focus also might include certain identifiable intangible assets) and do not see goodwill as an asset. Some of those users were open to a direct write-off of goodwill, but some highlighted that disclosures would have to provide a history of the capital invested in acquisitions for investment return calculations. Some users were open to the idea of a direct write-off over amortization primarily because it would not require an adjustment to an entity's reported results each reporting period.

19. The staff notes that the feedback from users that goodwill impairment is not used quantitatively, but can be helpful qualitatively, is consistent with the feedback the FASB received in connection with outreach performed when the qualitative screen was developed in 2011. An outreach summary from February 2011 on that project indicated that users were fairly indifferent about the manner in which goodwill is assessed for impairment but they

would support any change that reduces costs incurred by preparers if it achieves a similar result from applying current guidance. Overall, the staff believes that users have been more outspoken in current outreach about the qualitative benefits of goodwill impairment and that may be due to the fact that amortization or a direct write-off would not achieve a result similar to current guidance.

20. Users of NFP financial statements indicated that they rarely see goodwill (because many NFPs either write goodwill off at the time of acquisition or do not recognize it due to qualifying as a merger), but when they do see it, the balances and impairment generally are not relevant to their analysis of NFPs. Many NFP stakeholders, including the members of the NAC and the AICPA Not-For-Profit Entities Expert Panel, support the extension of the PCC alternative to NFPs because they believe that NFPs and private companies face similar challenges (for example, they do not have an observable market price, they do not apply the segments guidance, which is the basis for reporting unit determination, and they have limited resources). At the March 10, 2014, NAC meeting, members were split on whether they preferred direct write-off or amortization of goodwill. However, all of the NAC members who spoke at the meeting supported a change from the current impairment model. Many comment letter respondents to the PCC alternative for goodwill also supported extending the private company alternative to NFPs.

International Studies

21. The European Financial Reporting Advisory Group (EFRAG), the Organismo Italiano di Contabilità (OIC), and the Accounting Standards Board of Japan (ASBJ) (collectively, the Research Group) conducted surveys and outreach to collect information related to the relevance of the impairment-only approach for goodwill. The Research Group published the results of those surveys and conclusions reached in its Discussion Paper, *Should Goodwill Still Not Be Amortised? Accounting and Disclosure for Goodwill*.[3]

[3] Click here for the Discussion Paper, *Should Goodwill Still Not Be Amortised? Accounting and Disclosure for Goodwill*.

Results of the EFRAG and OIC Survey

22. The EFRAG and the OIC conducted an international survey that focused on the usefulness of the financial information under current guidance on accounting for goodwill, the costs and complexity of the impairment test, and the ability to audit the impairment test.[4]

23. The study indicated that users had mixed views about what is included in goodwill and whether the information is used. Users also had mixed views about the usefulness of goodwill impairment. While some thought it provided useful information on projections for each cash-generating unit, others noted that the usefulness of the information was limited because users expected impairment before it was recognized.

24. A slight majority of respondents agreed conceptually with only reducing the value of goodwill on impairment.

25. In addition, a slight majority of the respondents indicated that the cost and complexity of the impairment model is significant. Suggestions to reduce costs included allowing amortization, limiting the impairment test to when an indication of impairment is present, reducing the frequency of the impairment test, requiring an impairment test only when the book value of equity compared with the market capitalization of the company exceeds a specified amount, introducing a less prescriptive approach, and clarifying the requirements.

26. A slight majority of respondents indicated that estimating the recoverable amount of goodwill in an impairment test is more difficult than estimating its useful life (if amortization was used).

27. Practitioners had mixed views about the auditability of the impairment test. Some thought it was no more difficult to audit than other management estimates included in the financial statements, while others found it difficult to challenge management's assumptions for future cash flows.

[4] EFRAG and OIC outreach results begin on page 12 of the Discussion Paper, *Should Goodwill Still Not Be Amortised? Accounting and Disclosure for Goodwill*.

Results of the ASBJ Outreach (Including Information Used for This Study and for PIR)

28. In response to the IASB's Request for Information on the Post-Implementation Review (PIR) of IFRS 3, *Business Combinations*, and in connection with the Research Group's study, the ASBJ performed outreach that included users, preparers, and auditors of both. GAAP and IFRS, since both standards are generally consistent in this area.[5] The ASBJ's outreach determined the following:

    (a) A significant majority of stakeholders believe there are shortcomings under the impairment-only approach. Users noted that impairment charges often occurred later than market participants expected and often are disregarded.

    (b) Stakeholders also highlighted challenges under the current guidance related to the subjectivity and unexpected costs of impairment testing.

    (c) Stakeholders noted that management had too much discretion in determining how to allocate goodwill.

    (d) Some users and most preparers supported the reintroduction of using both amortization and impairment, because they consider this approach to (1) provide a better representation of the economic substance of goodwill (that it is consumed and replaced with internally generated goodwill as time passes) and (2) better enable the matching of business combination expenses and revenues in periods after the business combination.

    (e) Many preparers noted that it is possible to estimate a reasonable period of amortization, but they favored setting a maximum amortization period. They suggested 20 years as a reasonable maximum period. Some preparers favored straight-line amortization as the most appropriate method for calculating amortization.

29. The FASB staff and Board members have had several discussions with the ASBJ over the last year about the subsequent measurement of goodwill. The feedback that the ASBJ has provided directly to the FASB is consistent with the information in the study described above.

[5] ASBJ outreach results begin on page 15 of the Discussion Paper, *Should Goodwill Still Not Be Amortised? Accounting and Disclosure for Goodwill*.

Conclusions in EFRAG Study

30. Because of questions raised about the usefulness of goodwill impairment and the cost and complexity of the impairment test, the Research Group explored other alternatives for the subsequent accounting for goodwill and reached the following conclusions:

    (a) An amortization and impairment approach for goodwill is appropriate, and it can be applied with a sufficient level of verifiability and reliability.

    (b) Current aspects of the impairment test can be improved.

    (c) Disclosures related to the impairment test can be improved.

Amortization and Impairment Approach

31. The Research Group believes that the reintroduction of goodwill amortization would be appropriate and noted the following:

    (a) It reasonably reflects the consumption of an economic resource over time and can be applied in a way that achieves an adequate level of verifiability and reliability.

    (b) The determination of a useful life would be subjective and the actual pattern of consumption may be difficult to predict.

        (1) The study considers a principle that goodwill should be amortized over the period in which it is expected to contribute to cash flows.

        (2) Application guidance would indicate that preparers should use all relevant information, giving greater consideration to objective evidence.

        (3) Factors to consider include the expected period of time in which an entity will have earnings from the acquisition and the residual useful life of the primary asset acquired.

        (4) The Research Group favored a rebuttable presumption that the useful life should not exceed 10 or 20 years.

    (c) Systematic amortization on a straight-line basis would be an appropriate balance between faithful representation and cost.

32. The Research Group also considered whether a discernable elements approach or a direct write-off were appropriate alternatives to the nonamortization of goodwill. The discernible elements approach separates acquired goodwill into different components (for example, the amount paid for synergies, the value of intangibles not separately recognized, the fair value of the "going concern" of the business, and overpayments or underpayments by the acquirer) and applies different treatments to the components. While this approach has some conceptual appeal to those involved with the study, it would be difficult to apply in practice because it requires numerous subjective judgments to identify the discernible elements, and it would likely not result in reduced costs or complexity.

33. Because goodwill is a resource controlled by an entity, results from a past event, and leads to future economic benefits (albeit in combination with other assets, which will contribute indirectly to future cash flows), the Research Group concluded that goodwill meets the definition of an asset in the IASB's *Conceptual Framework for Financial Reporting*. The group also concluded that because goodwill had value at day one, the value at day two should not be zero; therefore, an immediate write-off approach would not be appropriate.

Improving the Impairment Test

34. To improve the impairment test, the study suggests focusing on implementation guidance to assist with:

    (a) The identification of cash-generating units

    (b) The inputs and methods used to determine the recoverable amount of the cash-generating units

    (c) The determination of the discount rate.

Improving Disclosures

35. The study concluded that there is room for improvement in the disclosure requirements. Disclosures discussed included:

    (a) Information about the assumptions, including the time horizon of expected cash flows and the inputs to the discount rate

(b) Information about the reasonableness of past assumptions, such as disclosing variances between forecasts and actual results to help investors assess the entity's ability to make accurate and precise forecasts

(c) Disclosures to assist in predicting the likelihood of a future impairment by providing information related to the performance of an acquired business, management's expectation of goodwill consumption, and characteristics of the acquisition.

36. The Research Group did not conclude the above disclosures should all be required, but, rather, that the interest in such disclosures warrants a need to reconsider user needs and reach an appropriate balance of disclosures to meet those needs.

Feedback Received on the Discussion Paper

37. The Research Group received 29 comment letters on the Discussion Paper, and jointly published a feedback statement[6] summarizing those comments on February 4, 2015. According to the feedback statement, most respondents agreed that the impairment-only model for acquired goodwill was not the most appropriate solution for subsequent measurement and agreed with the idea of reintroducing amortization of goodwill. Respondents' views on whether the IASB should indicate a maximum amortization period were mixed. Respondents also pointed out that there are areas for improvement in the impairment testing. They had mixed views on whether disclosure requirements on impairment tests could be improved. Many respondents indicated that if amortization was reintroduced, the relevance of impairment and related disclosures would significantly decrease.

Japan's Modified International Standards

38. In July 2014, the ASBJ proposed modified international accounting standards for Japanese reporting entities in its Exposure Draft, *Japan's Modified International Standards (JMIS): Accounting Standards Comprising IFRSs and the ASJB Modifications*. Those modified

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[6] Click here for the Feedback Statement: *Responses to the Discussion Paper*, Should Goodwill Still Not Be Amortised? Accounting and Disclosure for Goodwill.

standards were approved and issued in June 2015. The modified international accounting standards primarily result in the use of IFRS, but include certain modifications. ASBJ Modification Accounting Standard No. 1, *Accounting for Goodwill*, addresses the accounting for goodwill.

39. Under ASBJ Modification Accounting Standard 1, goodwill is to be amortized using a systematic basis (straight line or another reasonable method) over its useful life, with the useful life not to exceed 20 years, and the amortization charge recognized in profit or loss. The amortization method and the useful life for goodwill is determined separately for each business combination. The ASBJ Modification Accounting Standard modifies disclosure requirements as well, requiring that entities disclose (a) the amortization method and the useful life for the goodwill, (b) the line item(s) in the profit and loss statement that include amortization, and (c) a reconciliation of the carrying amount of goodwill at the beginning and end of the period, showing separately the gross carrying amount and accumulated amortization (aggregated with accumulated impairment losses), in addition to other disclosure requirements under IFRS 3.

40. Consistent with current IFRS guidance, goodwill is tested for impairment annually according to the IFRS impairment model. In the ASBJ Modification Accounting Standard's basis for conclusions, the ASBJ considered whether the requirements for the impairment test should be modified. The general principle for impairment testing under IFRS is that the recoverability of goodwill should be tested only when there is an indication of impairment. Because goodwill is not amortized under IFRS, the requirement for annual impairment testing is an exception to that principle. Although some ASBJ stakeholders argued that, because goodwill is being amortized under the modified standard, it should be tested only when there is an indication of impairment, the ASBJ ultimately decided to minimize changes to IFRS and left the requirements for the annual impairment test unchanged.

Staff Analysis and Options

41. The history above illustrates that many models have been considered for the subsequent measurement of goodwill. Throughout the FASB staff's current outreach, review of

comment letter responses, and outreach on prior projects, the feedback on the accounting for goodwill has consistently been mixed. There does not appear to be a clear answer on what the accounting for goodwill should be, and it may be challenging to identify a model that satisfies the needs of all stakeholders.

42. It also is possible that all of the potential benefits from the optional qualitative test for goodwill impairment have not been realized because the guidance is new (because the amendments in Update 2011-08 were issued in late 2011, companies had only been able to use the qualitative test once or twice at the time of the FASB staff's outreach) and the global economy has been recovering to some extent from a recession (which should begin to decrease the risk of impairment for many companies). The staff observes that feedback about the complexity of asset impairment testing during or immediately following an economic recession is to be expected and is not necessarily a sufficient reason to immediately make a significant change to the accounting model. Furthermore, the 2014 Duff & Phelps study referenced above indicates that the use of the qualitative screen has increased in recent years.

43. The FASB requested that the staff analyze each of the following four potential views on the subsequent measurement of goodwill:

    (a) View A: PCC model

    (b) View B: Amortize goodwill

    (c) View C: Direct write-off

    (d) View D: Simplified impairment test.

44. The FASB is still considering these alternatives and the results of the staff research, and has not yet made a decision.

View A: PCC Model

45. The private company alternative allows an entity to:

    (a) Amortize goodwill over 10 years or less than 10 years if an entity demonstrates that another useful life is more appropriate.

(b) Make an accounting policy election to perform its impairment testing at the entity level or the reporting unit level.

(c) Test goodwill for impairment only when a triggering event occurs that indicates the fair value of an entity (or a reporting unit) may be below its carrying amount.

(d) Retain the option to first assess qualitative factors to determine whether a quantitative impairment test is necessary.

(e) Eliminate step two of the quantitative test.

(f) Record goodwill impairment, if any, as the excess of the entity's (or the reporting unit's) carrying amount over its fair value. Goodwill should not be reduced below zero.

46. Goodwill existing at the beginning of the period of adoption will be amortized prospectively over 10 years or less than 10 years if the entity demonstrates that another useful life is more appropriate. Early adoption is permitted for all financial statements that have not yet been made available for issuance. The PCC also reached a consensus-for-exposure at its July 21, 2015 meeting to provide private companies with an unconditional one-time option to elect a PCC alternative without having to conduct an initial preferability assessment.

47. Proponent and opponent views of different aspects of the PCC alternative are discussed in various views below. Some stakeholders in the FASB staff's outreach who support amortizing goodwill do not support certain aspects of the PCC alternative that were designed, in part, to reduce cost and complexity on the basis that users generally would ignore goodwill amortization. Some believe that an amortization model should require a reporting entity to consider its own facts and circumstances to estimate the useful life of goodwill (versus permitting the use of an arbitrary period) and in the determination of how goodwill impairment at the reporting unit level (or entity level) is allocated to the goodwill of each acquisition (versus permitting a pro rata approach). Users generally did not feel strongly about the specific aspects of an amortization model, because any amount of amortization would be ignored. However, based on the PBE users' preference for impairment, the staff believes that they would prefer any aspect of the model that would make impairment charges more meaningful.

View B: Amortize Goodwill

48. Key elements include the following:

    (a) Amortize goodwill over its expected useful life, not to exceed certain number of years

    (b) Periodic impairment tests.

49. Proponent views include the following:

    (a) Goodwill is acquired to generate future cash flows and should be recognized as those cash flows are realized.

    (b) Amortization is conceptually inferior to an impairment model, but users often disregard goodwill impairment charges in their quantitative analyses of operating performance.

    (c) The benefits of the current impairment model do not justify its costs.

    (d) Goodwill is a wasting asset and the internally generated goodwill that is replacing it is not recorded.

50. Opponent views include the following:

    (a) At least part of goodwill is a nonwasting asset and can have an indefinite useful life.

    (b) The useful life and the pattern in which any wasting portion of goodwill diminishes are difficult to estimate and are highly subjective and may not be comparable among entities.

    (c) Amortization of goodwill decreases the relevance of financial statements.

    (d) Amortization of goodwill is unfair to entities whose growth comes largely from acquisitions rather than from internal sources.

    (e) Goodwill does not necessarily directly correlate to cash paid to benefit future operations.

51. There are several specific issues that also would need to be addressed under View B as follows:

    (a) Useful life:

        (1) Selected based on facts and circumstances

        (2) Prescribed

(i) Ten years (PCC alternative)

(ii) Fifteen years (useful life of goodwill for tax)

(iii) Twenty years (1999 Exposure Draft)

(iv) Forty years (APB Opinion 17)

(b) Pattern of recognition:

(1) Straight line

(2) Systematic and rational

(c) Impairment test:

(1) Current GAAP (annual 2-step approach)

(2) Simplified (see View D below)

(d) Allocation of impairment among amortizable units of goodwill:

(1) Reasonable and rational approach

(2) Pro rata

(e) Allocation of goodwill on disposal (amount disposed and reallocation of remaining amount):

(1) Reasonable and rational approach

(2) Relative fair value approach

(f) Reorganization of reporting units:

(1) Reasonable and rational approach

(2) Current GAAP (relative fair value).

View C: Direct Write-Off

52. Key elements include the following:

(a) Write off goodwill at transition

(b) Write off any new goodwill at the acquisition date as any of the following:

(1) A charge to net income

(2) A charge to other comprehensive income

(3) An adjustment directly to equity.

53. Proponent views include the following:

(a) Users ignore goodwill and its subsequent measurement (impairment or amortization).

(b) Direct write-off could eliminate all costs associated with the subsequent measurement of goodwill.

(c) Any model for amortizing goodwill would result in an amortization period that is arbitrary and would require ongoing impairment tests.

(d) Concerns about how reliably goodwill can be measured after acquisition and/or uncertainties about what the asset and subsequent measurement represents.

(e) Lack of comparability arises today between similar companies as a result of recognizing goodwill as an asset in a business combination versus internally generated goodwill.

(f) Others assert that goodwill is not an asset because:

(1) It cannot be used to settle liabilities.

(2) There is no observable market for it.

(3) It cannot be transferred separately from the entity.

(4) Its useful life is unclear.

(5) It is a residual.

(g) They argue that the fact that a buyer is willing to pay for goodwill (or pay more than the fair value of the net assets separately recognized in a business combination) in an arms-length transaction and that it may contribute to future cash flows does not necessarily mean that it is an asset or that it provides relevant information about an acquisition. Proponents point to examples of expenditures that are made for the purpose of generating future cash flows but that are generally expensed as incurred, such as advertising and research and development costs. While entities make those expenditures with an expectation of generating cash inflows, they do not give the entity a present right to such cash inflows.

54. Opponent views include the following:

(a) Goodwill has the characteristics of an asset in FASB Concepts Statement No. 6, *Elements of Financial Statements*.

(b) Goodwill is controlled by the acquirer and it contributes to the generation of future cash flows much like other intangible assets or long-lived assets. In connection with the development of FASB Statement No. 141 (revised 2007), *Business Combinations*, the FASB also concluded that goodwill is an asset and, therefore, should not be written off at the date of acquisition.

(c) If goodwill had value initially (which opponents believe is evident from the purchase price a buyer is willing to pay in a business combination), no event other than a catastrophe could render goodwill immediately worthless.

(d) A business as a whole is an asset, thus, the value of that asset should be recorded, in total, on the acquirer's balance sheet when it is purchased. It is inappropriate to treat the purchase of a business differently in a business combination versus an investment in a smaller portion of the business.

(e) There are difficulties that arise in determining the decline in the value of goodwill in subsequent periods, but such estimation difficulties are not unique to goodwill and are not used as a justification for the immediate write-off of other assets.

(f) Goodwill should continue to be tested for impairment, at least annually, because impairment is a relevant indicator of the success or failure of an acquisition and/or management.

(g) Writing off goodwill could negatively affect some companies' net assets/equity and could cause a perception that a business is not being managed appropriately (amortization over a short period could have a similar effect).

(h) Ratios or debt covenants that include measures based on total assets or equity could be affected by the direct write-off of goodwill, and the potential need to amend debt agreements could add costs to the system.

(i) Preparers and NAC members generally did not support any disclosures associated with the performance of an acquisition that could be required under the direct write-off approach.

55. Recognition in other comprehensive income or equity also has additional issues that would need to be addressed:

(a) Allocation of goodwill upon a disposal

(b) Classification of bargain purchase gains.

View D: Simplified Impairment Test

56. Potential simplifications for the impairment test identified by the staff include any of the following:

(a) Testing for impairment at the entity, operating segment, or reportable segment level rather than the reporting unit level

(b) Using a one-step quantitative test rather than a two-step test

(c) Testing for impairment only on the occurrence of a triggering event rather than annually

(d) The ability to change the date the impairment test is performed rather than a requirement to test at the same time every year.

57. Proponent views include the following:

(a) An amortization model would not provide decision-useful information and would make the income statement less relevant.

(b) A direct write-off approach may reduce the relevance of the financial statements to some investors who are interested in return on assets, return on equity, or other ratios that would be affected by a direct write-off of goodwill.

(c) Simplifying the impairment model could reduce costs without significantly changing the usefulness of the financial statements.

(d) Many users of PBEs are more interested in the existence of impairment than the precise amount.

(e) A simplified impairment test model also could be adopted in conjunction with the amortization approach in View B.

58. There are several specific issues that also would need to be addressed under View D as follows:

(a) Level at which goodwill impairment should be tested

(1) Reporting unit

(2) Operating segment

(3) Reportable segment

(4) Entity level

(b) Method of allocating goodwill upon disposal (if the testing level is changed)

(1) Retain current GAAP

(2) Reasonable and rational approach

(c) Impairment test

(1) One step

(i) Use assets and operating liabilities for entities with zero or negative carrying value

(ii) Require step two for entities with zero or negative carrying value (if they meet qualitative factors)

(iii) Write off goodwill for entities with zero or negative carrying value (if they meet qualitative factors)

(2) Two step (current GAAP)

(3) Retain qualitative screen

(4) Frequency

(i) Annually, at same date every year (current GAAP)

(ii) Annually

(iii)Only on occurrence of triggering event.

Alternative or Requirement for Public Business Entities

59. The last issue that the staff identified for the FASB to consider is whether any change to the accounting for the subsequent measurement of goodwill should be required or optional for PBEs. The PCC alternative is optional for private companies.

60. Proponents of making any changes optional think there is no good answer to the question on subsequent measurement of goodwill, and they do not think subsequent measurement provides much information to users. Therefore, proponents think an entity should be able to select the option it believes is most appropriate. Opponents to having an option think it would negatively affect comparability of GAAP financial statements. They think because goodwill can be quantitatively significant, different approaches can dramatically affect net income.

61. Some respondents to the FASB's 2001 Exposure Draft on an annual goodwill impairment test (and on eliminating goodwill amortization) suggested that entities should have the option to amortize goodwill or be able to do so in certain circumstances. The FASB concluded at that time that such an approach should not be permitted because it would decrease comparability in financial reporting.