FASB FINANCIAL ACCOUNTING STANDARDS BOARD®

	Memo No.	**18B**
MEMO	Issue Date	**June 8, 2018**
	Meeting Date(s)	**Joint BM June 19, 2018**

Contact(s)	**Joy Sy**	Lead Author/Project Lead	Ext. 358
	Francesca Roberts	Co-Author	Ext. 384
	Jeffrey Mechanick	Assistant Director	Ext. 301

Project	**Accounting for Certain Identifiable Intangible Assets in a Business Combinations and Subsequent Accounting for Goodwill for Public Business Entities and Not-for-Profits**
Project Stage	**Pre-agenda**
Issue(s)	**History, Background, and Current Stage of the FASB's Research Project**

Memo Purpose

1. This memo will be used at a non-decision-making meeting of the International Accounting Standards Board and the Financial Accounting Standards Board (the FASB). The purpose of this memo is to summarize the history and background of the requirements in GAAP on the accounting for intangible assets and subsequent accounting for goodwill. This memo also discusses the project currently on the FASB's research agenda that is examining these topics.

Structure of the Paper

2. The paper is structured as follows:
   (a) History of Goodwill and Intangible Assets
   (b) Background of the Research Project
   (c) Current Stage of the Research Project.

History of Goodwill and Intangible Assets

3. Amortization of goodwill was part of GAAP for more than 30 years (since 1970) under APB Opinion No. 16, *Business Combinations*. The FASB eliminated the amortization of goodwill when it issued FASB Statement No. 141, *Business Combinations*, and FASB Statement No. 142, *Goodwill and Other Intangible Assets*, in 2001. One reason why the FASB undertook Statements 141 and142 was because the two acceptable methods of accounting for business combinations—the pooling-of-interests and purchase methods—produced dramatically different financial results despite representing economically similar transactions. The FASB at the time concluded that the information provided by the pooling method was less relevant in terms of completeness, predictive value, and feedback value.

4. Additionally, entities that could not meet the conditions to apply the pooling-of-interests method and had to apply the purchase method thought they were at a disadvantage compared with those that could meet the conditions for pooling of interests. This view of an unlevel playing field also extended internationally. For these reasons and others, the FASB decided to retain only the purchase method, now termed the acquisition method, that results in recognition of goodwill.

5. Because feedback from financial statement users indicated that goodwill amortization expense was not useful information in analyzing investments and because the FASB considered the presumption that goodwill has an indefinite useful life, the FASB removed the requirements to amortize goodwill, and instead required goodwill to be tested at least annually for impairment.

6. Related to goodwill is the identification of intangible assets. Increased merger and acquisition activity created user demand for more information about acquired intangible assets. Consequently, the contractual-legal and separability criteria were developed to distinguish identifiable intangible assets from goodwill.

7. At the time, Statements 141 and 142 were considered an important step in the process of achieving greater convergence of cross-border accounting. The basis for conclusions of both Statements describe the anticipated reduction in costs borne by preparers, auditors, and users of financial statements alike, as well as facilitation of the efficient allocation of capital globally.

8. The FASB issued FASB Statement No. 141 (Revised 2007), *Business Combinations*, which broadened the scope of the standard and improved the comparability of information about business combinations provided in financial reports. Statement 141(R), along with the IASB's IFRS 3, *Business Combinations*, completed a joint effort by the FASB and the IASB to promote convergence in accounting for business combinations.

9. What may not have been anticipated by Statements 141, 142, and 141(R) was the increased cost and complexity added to the goodwill impairment test from the subsequent issuance of FASB

Statement No. 157, *Fair Value Measurements*, in 2006. Statement 157 defined the term fair value (as an exit price), established a framework for measuring fair value, and expanded disclosures about fair value measurements. A result was increased scrutiny of the valuation of assets and liabilities, particularly those that do not have readily determinable fair values (level 2 and level 3 type assets and liabilities). This in turn increased the use of valuation experts. The Post Implementation Review of Statement No. 141(R) in 2013 identified and described the widespread increase in cost and complexity; it increased costs borne by preparers and ultimately users, and it also significantly affected auditability. In an effort to simplify and reduce cost and complexities, the FASB issued Accounting Standards Update No. 2017-04*, Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*, which eliminated Step 2 of the impairment test for all entities. The elimination of Step 2 removed the need to assign fair value to all of the assets and liabilities of a reporting unit and to calculate the implied fair value of goodwill.

10. The FASB also issued alternatives, as described below, to accounting for goodwill and certain intangible assets to reduce cost and complexities for private companies.

Background of the Research Project

11. Accounting Standards Update No. 2014-02, Intangibles—Goodwill and Other (Topic 350): Accounting for Goodwill, and Accounting Standards Update No. 2014-18, Business Combinations (Topic 805): Accounting for Identifiable Intangible Assets in a Business Combination, simplified the requirements for private companies in relation to accounting for goodwill and intangible assets. The amendments in the Updates provide private companies with the option to:

    (a) Amortize goodwill on a straight-line basis over 10 years or less, if the entity demonstrates that another useful life is more appropriate. For private companies that elect to amortize goodwill, impairment testing would be performed upon a triggering event, rather than annually, and can be performed at the entity level or at the reporting unit level.

    (b) Subsume certain intangible assets (those that cannot be sold or licensed independently from the business) and all non-compete agreements into goodwill and amortize goodwill.

12. Presently, the project on the FASB's research agenda examines the possibility of extending some or all of these private company alternatives to public business entities, not-for-profits, and potentially to private companies who have not elected the alternatives. This research project also considers and evaluates whether additional changes to the subsequent accounting for goodwill beyond any changes to the impairment test resulting from Update 2017-04 are appropriate.

13. The FASB has previously undertaken projects relating to goodwill and intangible assets separately. However, as a result of the agenda consultation in September 2017, the FASB combined the following two projects into one and added it to its research agenda:

(a) Subsequent Accounting for Goodwill for Public Business Entities and Not-For-Profit Entities; and

(b) Accounting for Identifiable Intangible Assets in a Business Combination for Public Business Entities and Not-For-Profit Entities.

14. The FASB also added a disclosure review project on intangible assets to its research agenda to examine the current disclosure requirements to improve the financial information in notes to the financial statements.

Current Stage of the Research Project

15. As discussed above, the objective of the research project is to determine whether certain or all elements of the private company alternatives issued in Update 2014-02 and Update 2014-18 should be extended to public business entities and not-for-profit organizations.

16. As part of the project, the staff is performing outreach to evaluate whether additional changes to the subsequent accounting for goodwill beyond any changes to the impairment test resulting from Update 2017-04 are appropriate.

17. The FASB plans to begin discussion on its research project in the third quarter of 2018 after further discussing the issues with its advisory groups and stakeholders.