

July 16, 2013

FASB's Private Company Council: Proposed Accounting Alternative – Goodwill

SUMMARY OF PROPOSAL

- The Financial Accounting Standards Board (FASB), through its Private Company Council (PCC), issued a proposed alternative within U.S. generally accepted accounting principles (GAAP), that would permit amortization of goodwill (the residual asset recognized in a business combination after recognizing all other identifiable assets acquired and liabilities assumed) and a simplified goodwill impairment model.
- Currently, under GAAP goodwill is not amortized but tested for impairment at least annually or more
 frequently if certain conditions exist. A company can choose to first perform a qualitative
 assessment to determine if it is more likely than not that a reporting unit's fair value is less than its
 carrying value, or it can bypass the qualitative assessment and proceed directly to step one and
 compare the carrying value of the reporting unit with its fair value.
- If the carrying value exceeds fair value, step two (which compares the implied fair value of the reporting unit's goodwill with its carrying value) must be performed to determine the amount of the goodwill impairment, if any. This necessitates performing a hypothetical application of the acquisition method under Topic 805 (also referred to as the purchase price allocation) to determine the implied fair value of goodwill and requires fair value measurement of the reporting unit's identifiable assets and liabilities.
- Under the proposed accounting alternatives, a company that elects the accounting alternative within GAAP would amortize goodwill over the useful life of the primary asset (the long-lived asset that is the most significant asset acquired in a business combination), not to exceed 10 years.
- Goodwill would be tested for impairment only when a triggering event occurs that would more likely than not reduce the fair value of a company below its carrying amount.
- Further, goodwill would be tested for impairment at the companywide level as compared to the
 current requirement to test at the reporting unit level. Step two of the current impairment test, which
 requires the application of a hypothetical purchase price allocation to calculate the goodwill
 impairment amount, would also be eliminated. Instead, the goodwill impairment amount would
 represent the excess of the company's carrying amount over its fair value.
- The PCC believes that the proposed accounting alternative, when elected, would continue to provide decision-useful information to the users of private company financial statements, while reducing the cost and complexity associated with the current goodwill impairment test.
- FASB is accepting comments until August 23; please send comments to CUNA by August 16.

DESCRIPTION OF PROPOSAL

Who Would Be Affected by the Amendments in This Proposed Update?

The proposed amendments would be available to an entity that recognizes goodwill in a business combination in accordance with Topic 805, Business Combinations, except for a publicly traded company or a not-for-profit entity as defined in the Master Glossary of the FASB Accounting Standards Codification. An entity within the scope of the proposed amendments that elects to apply the accounting alternative in this proposal would be subject to all of the related subsequent accounting and disclosure requirements within the accounting alternative. The accounting alternative, if elected, would apply to all existing goodwill and to all new goodwill generated in business combinations entered into after the effective date of this proposal.

How Would the Proposed Alternative Differ from Current GAAP?

Currently, GAAP requires goodwill of a reporting unit to be tested for impairment at least annually or more frequently if certain conditions exist. An entity can choose to first perform a qualitative assessment to determine if it is more likely than not that a reporting unit's fair value is less than its carrying value, or it can bypass the qualitative assessment and proceed directly to step one and compare the carrying value of the reporting unit with its fair value. If the carrying value exceeds fair value, step two must be performed to determine the extent of goodwill impairment. Step two compares the implied fair value of the reporting unit's goodwill with its carrying value. This necessitates performing a hypothetical application of the acquisition method (purchase price allocation) to determine the implied fair value of goodwill after measuring the reporting unit's identifiable assets and liabilities in accordance with Topic 805.

Under the proposed amendments, an entity that elects the accounting alternative within GAAP would amortize goodwill on a straight-line basis over the useful life of the primary asset acquired in a business combination, not to exceed 10 years. Goodwill would be tested for impairment only when a triggering event occurs that would indicate that the fair value of an entity may be below its carrying amount. Further, goodwill would be tested for impairment at the entity-wide level rather than at the reporting unit level. The PCC further simplified goodwill impairment by eliminating step two of the current impairment test, which requires the application of a hypothetical purchase price allocation to calculate the goodwill impairment amount. The goodwill impairment amount would represent the excess of the entity's carrying amount over its fair value.

The PCC believes that the proposed accounting alternative, when elected, would continue to provide decision-useful information to users of private company financial statements, while reducing the cost and complexity associated with the current goodwill impairment test. The PCC received input indicating that most users of private company financial statements disregard goodwill and goodwill impairment losses in their analysis of a private company's financial condition and operating performance. Accordingly, the PCC believes that the proposed amendments would result in minimal loss of relevant information for users of private company financial statements.

The PCC believes that the proposed amendments would reduce the costs and complexity of accounting for goodwill and, therefore, would reduce the cost and complexity of preparing financial statements. The amortization method and the relief from the requirement to test goodwill for impairment at least annually would result in significant cost savings for many private companies that carry goodwill on their balance sheet, because amortization would reduce the likelihood of impairments, and companies would be required to test goodwill for impairment only when a triggering event occurs. Testing goodwill for impairment on an entity-wide basis would further reduce cost and complexity. Moreover, even if goodwill is impaired, determining the amount of the impairment under the accounting alternative would not involve the application of a hypothetical purchase price allocation, which is costly and complicated but, instead, would be determined as the amount by which the carrying amount of the entity exceeds its fair value.

Overall, the PCC believes that the accounting alternative for goodwill is responsive to the unique needs of private companies and their stakeholders. The PCC believes that the accounting alternative for goodwill would continue to provide decision-useful information to users of private company financial statements, while providing a reduction in the cost and complexity associated with the current goodwill impairment test. Therefore, the PCC believes that the proposed amendments meet the overall objective of the proposed Private Company Decision-Making Framework for addressing the unique needs of private company stakeholders.

CUNA Question 1: Would the proposed amendments reduce overall costs and complexity compared with existing guidance? If not, please explain why.

CUNA Question 2: Do you agree that the accounting alternative for goodwill would provide relevant and decision-useful information to users of private company financial statements? If not, what accounting alternative, if any, would provide relevant information to users?

CUNA Question 3: Do you agree with the PCC's decision to amortize goodwill on a straight-line basis over the life of the primary asset acquired in a business combination, not to exceed 10 years? If not, please tell us what alternative approach or useful life you would prefer?

CUNA Question 4: Do you agree that goodwill accounted for under this alternative should be tested for impairment at the entity-wide level? If not, should an entity be either required or given an option to test goodwill at the reporting unit level? What issues, if any, arise from amortizing goodwill at the individual acquired goodwill level while testing for goodwill impairment at the entity-wide level?

CUNA Question 5: Do you agree that goodwill accounted for under this alternative should be tested for impairment only upon the occurrence of a triggering event that would indicate that the fair value of the entity may be below its carrying amount? If not, when should goodwill be tested for impairment? Should there be an annual requirement to test goodwill?

When Would the Amendments Be Effective?

The accounting alternative for goodwill would be applied prospectively for all existing goodwill and for all new goodwill generated in business combinations after the effective date. The proposal does not include an effective date.

CUNA Question 6: Do you agree that the proposal should be applied on a prospective basis for all existing goodwill and for all new goodwill generated in business combinations after the effective date? Should retrospective application be permitted?

CUNA Question 7: The scope of this proposal uses the term publicly traded company from an existing definition in the Master Glossary. In a separate project about the definition of a nonpublic entity, FASB is deliberating which types of business entities would be considered public and would not be included within the scope of the Private Company Decision-Making Framework. FASB and PCC expect that the final definition of a public business entity resulting from that project would be added to the Master Glossary and would amend the scope of this proposal. FASB has tentatively decided that a public business entity would be defined as a business entity meeting any one of the following criteria:

- a) It is required to file or furnish financial statements with the Securities and Exchange Commission.
- b) It is required to file or furnish financial statements with a regulatory agency in preparation for the sale of securities or for purposes of issuing securities.
- c) It has issued (or is a conduit bond obligor) for unrestricted securities that can be traded on an exchange or an over-the-counter market.
- d) Its securities are unrestricted, and it is required to provide GAAP financial statements to be made publicly available on a periodic basis pursuant to a legal or regulatory requirement.

Do you agree with FASB's tentative decisions reached about the definition of a public business entity? If not, please explain why.

CUNA Question 6: Any other comments or questions.

Please send comments to Senior Assistant General Counsel <u>Luke Martone</u>.

Click <u>here</u> for the proposal.