Response to Invitation to Comment
Topic 2019 - 720

I am a former FASB Board member (1999 - 2007) involved in the education, deliberations and issuance of Statement 142 (codification topic 350) which eliminated the Amortization method for subsequent accounting for goodwill.

Subsequent Accounting for Goodwill

I am disappointed in the structure and content of this I to C. It simply lists concerns based on often stated positions without analysis of those concerns. It reads like a polling document (especially with the “Check the BOX” display on page 16). I doubt the input received on this document will be useful to the FASB staff or Board. It will be another poll of likes and dislikes.

I believe the I to C should be structured based the characteristics of useful financial information in Concept Statement 8. The major question should be which subsequent accounting approach provides RELEVANT information. To do this the listed assertions that the Impairment approach does not provide meaningful information should be questioned and responses requested on that effort. Thus the I to C should ask the following questions (I have given my responses to the questions).

1. Does the assertion that impairments are considered non-recurring (or non-cash charges) and often removed by investors or eliminated by non-GAAP displays a confusion of financial analysis for financial reporting?

   My response: Yes, just because an event does not often occur (or that the event does not directly affect cash) does not mean that the event should not be reported in the financial statements. Financial statement users use financial information in different ways. The creations of various metrics using information in the financial statements and elsewhere is financial analysis. The determination of the validity and usefulness of that data is the responsibility of the user and the presenter of that data. Accounting standards are designed to provide information, not determine how that information is used. Assertions that the multiplying practice of reporting entities presenting non-GAAP displays call for changes to GAAP is not supportable. Where would compensation, marketing and interest charges belong if not in the financial statements?

2. Does reporting goodwill impairment provide both confirmatory and predictive information?

   My response: YES, the confirmation information confirms that events have occurred that indicate the value of goodwill have decreased. It also provides important predictive information about expected future cash flows from the reporting unit that
includes the goodwill. The fair value of the reporting unit would not be reduced without a prediction that future cash flows will be less than previously expected or that there was a significant increase in the uncertainty about those cash flows. Is not the prediction of the value of future cash flows the goal of financial analysis?

3. Have not almost all events in financial statements already occurred? If "lagging" is meant as the reporting is "too long" after the events have occurred, is that not a problem with application of the accounting standard rather than the standard itself?

My response: Accounting usually reports events that have occurred. The outlier is the recently issued standard called CECL which anticipates events before they happen (and which I disagree with as I have stated in other comment letters). However, the use of fair value to measure and trigger goodwill impairment incorporates forward-looking information as of the reporting date to provide predictive information.

Management knows more about the reporting unit than anyone. If the reporting of an impairment is "too late", it is their application of the standard that should be improved.

4. Financial disclosures provide important information. But are disclosures without reporting in the financial statements an effective communication about goodwill impairment?

My response: No, consider how information about compensation with stock options became more effective when Statement 123 was replaced with 123 Revised (Codification topic 360). Disclosures are not an excuse to avoid reporting the effect of events.

5. Does subsequent accounting for goodwill by the Amortization method provide RELEVANT information?

My response: I believe goodwill amortization in the past and would be in the future is simply a mathematical number. It provides NO relevant information. Comments such as amortization reduces the chance there will be a goodwill impairment or that some private companies use the Amortization method do not make amortization meaningful.

During my education about subsequent accounting for goodwill leading to the elimination of amortization, I participated in a field visit with management that owned a subsidiary with significant goodwill and the management of the subsidiary. They told me they eliminated the amortization in evaluating the performance of the subsidiary because it provided NO financial information. They used the unamortized goodwill amount in evaluating the performance of the subsidiary. They expected a return on goodwill like that of the subsidiary’s other assets.
Based my responses to the question that should have been asked, I believe the impairment approach should be retained and the Amortization method should not be pursued. Amortization fails to meet the first characteristic of useful financial information. It does not provide Relevant information.

Should simplification of goodwill impairment be pursued? Evaluating the performance of reporting units can be complex and subjective. But that is what is expected of management and company’s Board of Directors. The elimination of step 2 has gone far in reducing the complexity and cost of dealing with impairment of goodwill. But it has also reduced the accuracy of identifying and measuring goodwill impairment. The use of the undiscounted cash flow trigger for recognizing impairment of long-lived assets (including intangible assets) pushes impairment onto goodwill rather than those assets. I accept that amendment to eliminate the second step of the impairment approach as a cost/benefit response but I don’t see other simplification changes.

RECOGNITION OF INTANGIBLES

In supporting the issuance of statements 141 and 141Revised (codification topic 805), I was focused on separating the reasons for the business combination from goodwill and communicating about those reasons. I admit I did not spend the time or effort to determine whether those reasons meet the definition of an asset in Concept Statement 6.

I suggest the staff and Board members evaluate the current practice on recognizing intangibles in a business combination against the tentative definition of an asset in their current Conceptual Framework project. If certain of those intangibles do not meet that definition, the Board should deliberate whether to keep them recognized or not. If not, how to best communicate the reasons for the acquisition and how those reasons work out.

I will be glad to meet with the FASB staff or Board to discuss my comments. Please contact me at ewtrott@gmail.com.