October 7, 2019

Technical Director
File Reference No. 2019-720
FASB
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Subject: Responses to Invitation to Comment regarding Identifiable Intangible Assets and Subsequent Accounting for Goodwill Released November 19, 2018

Dear Technical Director:

We appreciate the opportunity to submit this letter with Responses to the Invitation to Comment regarding Identifiable Intangible Assets and Subsequent Accounting for Goodwill Released November 19, 2018.

ValueKnowledge LLC is a professional services firm, founded in 2005. We frequently estimate the fair value of identifiable intangible assets acquired in a business combination in accordance with Financial Accounting Standards Board (FASB) ASC 820, Fair Value Measurement, and ASC 805, Accounting for Identifiable Intangible Assets in a Business Combination, for publicly traded and private clients, so we are very interested in the FASB’s invitation to comment regarding Identifiable Intangible Assets and Subsequent Accounting for Goodwill.

Summary of this comment letter: The relatively recent simplification of the impairment testing for goodwill is beneficial, including the introduction of “Step zero” qualitative testing and the elimination of the previously onerous Step 2 procedures.

Goodwill should not be amortized. Testing for impairment periodically is worthwhile. The current procedures to identify and measure the fair value of identifiable intangible assets are appropriate for the recording of acquired assets.
Our responses to the specific questions raised in the ITC follow.

1) **What is goodwill and what does it mainly represent?**

ValueKnowledge response: Under ASC 805, goodwill is currently quantified as a residual; it is purchase price minus acquired net assets. Goodwill can also be quantified with a present value of cash flows, by beginning with all the cash flow from the business and subtracting all the cash flows from the acquired net assets. When viewed as cash flows, most of the cash flows attributed to goodwill occur after the economic life of the identified intangible assets and other identified net assets. In a DCF of the business, the cash flows that most resemble the cash flows to goodwill would reside in the terminal value and have a perpetual growth assumption.

That’s what goodwill primarily is: the asset that represents the value of the potential for the business to continue indefinitely. In a going concern business, the DCF value that acquirers and sellers often rely on to understand the expected benefits of business ownership include the assumption of indefinite existence of that business. That assumption of indefinite existence of that business is implicit in almost every DCF-based business valuation. Goodwill, like the business, is expected to be perpetual and outlast the acquired depreciable and amortizable assets.

The ITC cited the underlying logic in Statement 142: “not all goodwill declines in value and for goodwill that does decline in value, it does not decline systematically over time. The Board also noted that goodwill may not be infinite lived, but it is indefinite lived.” I agree with that premise. Goodwill also includes workforce, going concern and other assets not quantified such as books and records, but those are minor considerations compared to the long-term ability of the business to continue past the decay of the current identifiable assets that make up the business.

2) **Do the benefits of the information provided by the current goodwill impairment model justify the cost of providing that information? Please explain why or why not in the context of costs and benefits.**

ValueKnowledge response: In our valuation practice, we have seen requests for valuations for impairment from our clients decline after the widespread implementation of the optional qualitative screen test, so the overall cost incurred is now appropriately focused on testing goodwill amounts that have the potential for impairment. Quantification of impairment, in our view, provides useful information to users of financial information to identify areas of financial distress that may otherwise be obfuscated, or information that companies that are at risk for impairment do not have financial distress that would demonstrate impairment. The cost to companies has
declined because of the optional qualitative screen test, and the information remains relevant and beneficial for users.

For example, an article by Tonya Garcia dated Aug 11, 2019 appearing in marketwatch.com observes: “Kraft Heinz Co. shares fell 14.5% in early Thursday trading after the food company released preliminary first-half results, indicating a steep earnings decline and more than $1.2 billion in impairment charges.” Although it is difficult to single out one reason for the stock price reaction, this impairment announcement and the related stock price change indicates that there is potentially significant information in impairment measurements.

3) On a cost-benefit basis, relative to the current impairment-only model, do you support (or oppose) goodwill amortization with impairment testing? Please explain why in your response.

ValueKnowledge response: Oppose. There will be less information for users of financial information if goodwill is subject to amortization. The cost of impairment testing has been mitigated with implementation the optional qualitative screen test.

4) If the Board were to decide to amortize goodwill, which amortization period characteristics would you support? Please include all that apply in your response and explain why you did not select certain characteristics.

a. A default period
b. A cap (or maximum) on the amortization period
c. A floor (or minimum) on the amortization period
d. Justification of an alternative amortization period other than a default period
e. Amortization based on the useful life of the primary identifiable asset acquired
f. Amortization based on the weighted-average useful lives of identifiable asset(s) acquired
g. Management’s reasonable estimate (based on expected synergies or cash flows as a result of the business combination, the useful life of acquired processes, or other management judgments).

ValueKnowledge response: A. or B. A long-term default period similar to APB 16, but longer, up to 50 years, may be reasonable to approximate the current reasonable practice of non-amortization of goodwill. In practice, I would expect that if a default period were adopted with some room for management’s reasonable adjustment if circumstances dictate (such as the acquisition of a company with an expectation of declining cash flow), companies would select the default period most frequently. This long-term amortization may protect the goodwill from some impairment, if impairment tests were still required, but would not reflect the indefinite nature of the goodwill asset as accurately as non-amortization.
5) Do your views on amortization versus impairment of goodwill depend on the amortization method and/or period? Please indicate yes or no and explain.

ValueKnowledge response: No. If amortization of goodwill were mandated, the accounting would not accurately reflect the indefinite nature of the goodwill asset. Any amortization method and/or period would similarly ignore the indefinite nature of the goodwill asset.

6) Regarding the goodwill amortization period, would equity investors receive decision-useful information when an entity justifies an amortization period other than a default period? If so, does the benefit of this information justify the cost (whether operational or other types of costs)? Please explain.

ValueKnowledge response: If the goodwill were to be amortized with other than a default period, I would expect that significant information would be obtained by equity investors. I hold the CFA credential and as a valuation firm we are users of financial information. In my example above, if the acquired company had an expectation of declining cash flow and selected a shorter amortization period for goodwill, which would be indicative of the expected life of the acquired operations. The incremental cost of assessing the reduced amortization period would be minimal, as that would likely be a significant consideration in the “deal model” or acquisition due diligence, and so the amortization period would be quantified during the deal team’s pre-acquisition procedures.

7) Do the amendments in Update 2017-04 (eliminating Step 2 of the goodwill impairment test) reduce the cost to perform the goodwill impairment test? Do the amendments in Update 2017-04 reduce the usefulness of financial reporting information for users? Please explain.

ValueKnowledge response: Yes, the amendments in Update 2017-04 meaningfully reduce the cost to perform the goodwill impairment test, specifically if Step 2 would have been required. The amendments in Update 2017-04 do not reduce the usefulness of financial reporting information for users. This was a useful simplification. The prior process of completing an entire ASC 805 process was burdensome, and although it sometimes provided a different outcome compared to post- Update 2017-04 results, both outcomes, in our experience, were typically directionally similar.

8) Do the amendments in Update 2011-08 (qualitative screen) reduce the cost to perform the goodwill impairment test? Do the amendments in Update 2011-08 reduce the usefulness of financial reporting information for users? Please explain and describe any improvements you would recommend to the qualitative screen.

ValueKnowledge response: The amendments in Update 2011-08 (qualitative screen) significantly reduced the cost to perform the goodwill impairment test. It is my understanding that the audit procedures related to this test could sometimes be
burdensome, however. Step 0 does not reduce the usefulness of financial reporting information for users.

9) Relative to the current impairment model, how much do you support (or oppose) removing the requirement to assess goodwill (qualitatively or quantitatively) for impairment at least annually? Please explain why in your response.

ValueKnowledge response: I fully support retaining the requirement to assess goodwill qualitatively or quantitatively approximately annually. Goodwill can be a large asset. Sometimes it diminishes in value because of economic, technological, competitive or industry changes. It cannot be assumed to be of full acquired value without testing occasionally, and annually is a useful interval. Companies are allowed to select their own testing date so that it is at a time of year most convenient for the organization, which is beneficial and shows flexibility in the guidance.

10) Relative to the current impairment model, how much do you support (or oppose) providing an option to test goodwill at the entity level (or at a level other than the reporting unit)? Please explain why in your response.

ValueKnowledge response: I oppose providing an option to test goodwill at the entity level (or at a level other than the reporting unit). It is my understanding that the original intent of testing at the reporting unit level, one level below segments, is to unearth information about potential financial distress that would otherwise be potentially buried in the consolidated operations. I also understand, however, that the testing at the reporting unit level sometimes becomes artificial, with the reporting units representing operations that are not managed separately so that balance sheets, PFI and other financial information have to be created especially for impairment testing. In those situations, the reporting units may coincide with the segments or the overall entity level.

11) What other changes to the impairment test could the Board consider? Please be as specific as possible.

ValueKnowledge response: See responses throughout this comment letter. No significant changes are suggested.

12) The possible approaches to subsequent accounting for goodwill include (a) an impairment-only model, (b) an amortization model combined with an impairment test, or (c) an amortization-only model. In addition, the impairment test employed in alternative (a) or (b) could be simplified or retained as is. Please indicate whether you support the following alternatives by answering “yes” or “no” to the questions in the table below. Please explain your response.
<table>
<thead>
<tr>
<th></th>
<th>Do You Support the Indicated Model? Yes/No</th>
<th>Do You Support Requiring an Impairment Assessment Only upon a Triggering Event? Yes/No</th>
<th>Do You Support Allowing Testing at the Entity Level or a Level Other Than the Reporting Unit?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Impairment only</td>
<td>yes</td>
<td>no: see response to question #9</td>
<td>no: see response to question #10</td>
</tr>
<tr>
<td>Amortization with impairment</td>
<td>yes</td>
<td>no: see response to question #9</td>
<td>no: see response to question #10</td>
</tr>
<tr>
<td>Amortization only</td>
<td>no</td>
<td>Not applicable</td>
<td>Not applicable</td>
</tr>
</tbody>
</table>

ValueKnowledge response: The current method of non-amortization and periodic testing for impairment is appropriate, as is was when the method was adopted in 2001. If changed to an amortization model (with amortization recognized over very long periods of time, say 50 years) periodic impairment testing would be appropriate. Testing upon a triggering event, as is the current practice, is also an appropriate and logical procedure because of the potential size of the goodwill asset, relative to total assets, and the potential for unexpected reduction in value. The cost of impairment testing has been appropriately reduced (see responses to #7 and #8).

13) Please describe what, if any, cost savings would be achieved if certain recognized intangible assets (for example, noncompete agreements or certain customer-related intangible assets) were subsumed into goodwill and amortized. Please be as specific as possible. For example, include specific purchase price allocation or subsequent accounting cost savings. Please list any additional intangible items the Board should consider subsuming into goodwill.

ValueKnowledge response: As a valuation firm, we have completed numerous valuations for use under Update 2014-18, referred to as the PCC rules. We have found that although we charge lower fees for the valuation of acquired identifiable intangible assets under PCC rules, that the amount of valuation effort is substantially similar. The effort is substantially similar because the PCC rules, as we understand them and have applied them, continue to require developing an understanding of the transaction, all the acquired assets, and quantifying the fair value of any contingent consideration as part of consideration transferred. PCC rules also require quantification of the workforce, tangible and working capital assets and other “non-subsumed” assets. Eliminating noncompete agreements and customer-related assets from the scope of the valuation work made accurate quantification of other potentially large identifiable intangible assets, such
as technology and tradename, significantly more uncertain. The fair value of those retained identifiable intangible assets was more uncertain because we had neither the quantification of the noncompete agreements and customer-related assets or, equally importantly, their related contributory asset charges, to give context to the value of the assets that remain to be quantified.

Based on the way the PCC rules have been implemented in practice, there is some minimal cost savings related to valuation fees. The reduced fees are not because of reduced effort by the valuation team but because of meeting client expectations of reduced fees for what appears to be, but is not, reduced effort.

As a valuation specialist, I cannot comment on reduced efforts or costs required by audit teams, if any, if the PCC rules were to be introduced into PBEs. However, the “half measures” represented by the valuation procedures under the PCC rules (specifically, eliminating noncompete agreements and customer-related assets) seem to raise auditor questions about what the value of identifiable intangible assets “would be under normal application of ASC 805 procedures”. The audit questions we have received on projects we have performed under PCC rules seem to seek the quantification of the noncompete agreements and customer-related assets and their related contributory asset charges, to give context to the value of the assets that remain to be quantified.

Our valuation team’s efforts were minimally reduced by application of the PCC rules.

14) Please describe what, if any, decision-useful information would be lost if certain recognized intangible assets (for example, noncompete agreements or certain customer-related intangible assets, or other items) were subsumed into goodwill and amortized. Please be as specific as possible. For example, include specific analyses you perform that no longer would be possible.

ValueKnowledge response: See response to #13, above. Without the quantification of all of the acquired identifiable intangible assets, the accurate quantification of other potentially large identifiable intangible assets, such as technology and tradename, is significantly more uncertain.

15) How reliable is the measurement of certain recognized intangible assets (for example, noncompete agreements or certain customer-related intangible assets)?

ValueKnowledge response: Judgement is involved in any valuation, especially in Level 3 measurements, making it unlikely that any two experienced valuation teams will arrive at exactly the same answer. However, assuming available facts and reliable data, measurement of the fair value of an intangible asset (for example, noncompete agreements or certain customer-related intangible assets) is reasonably reliable.
16) To gauge the market activity, are you aware of instances in which any recognized intangible assets are sold outside a business acquisition? If so, how often does this occur? Please explain.

ValueKnowledge response: Yes. Sales of intangible assets are readily observable outside of business combinations. Technology, trademarks and trade names, and customer lists, contracts and relationships are frequently sold.

17) Of the possible approaches presented, which would you support on a cost-benefit basis? Please rank the approaches (1 representing your most preferable approach) and explain why you may not have selected certain approaches.

a. Approach 1: Extend the Private Company Alternative to Subsume Certain CRIs and all NCAs into Goodwill
b. Approach 2: Apply a Principles-Based Criterion for Intangible Assets
c. Approach 3: Subsume All Intangible Assets into Goodwill
d. Approach 4: Do Not Amend the Existing Guidance.

ValueKnowledge response: D: Approach 4. Information would be lost if the existing guidance were amended.

18) As it relates to Approach 2 (a principles-based criterion), please comment on the operability of recognizing intangible assets based, in part, on assessing whether they meet the asset definition.

ValueKnowledge response: The principles-based criterion may lead to variation in valuation and measurement procedures that would reduce comparability of financial statements period to period and company to company. The asset definition already requires some judgement so changing the asset identification and measurement process to a principles-based criterion would affect the current practices and add complexity and uncertainty.

19) Approaches 1–3 assume that subsuming additional items into goodwill would necessitate the amortization of goodwill. Do you agree or disagree? Please explain why.

ValueKnowledge response: Yes. Identifiable intangible assets subsumed into goodwill would cause goodwill to contain amortizable assets in some proportion. As such, goodwill would take on some (but not all) attributes of the amortizable assets.

20) What is your assessment of the incremental costs and benefits of disclosing the facts and circumstances that led to impairment testing that have not led to a goodwill impairment loss?

ValueKnowledge response: If the procedures did not lead to recognizing impairment, I see minimal benefit to disclosing the facts.
21) What other, operable ideas about new or enhanced disclosures would you suggest the Board consider related to goodwill?

ValueKnowledge response: Consider a disclosure listing goodwill amounts arising from each acquisition and year it was recognized in the goodwill account, with potentially some grouping of similar acquisitions by year. This would provide context to the goodwill amount which may have accumulated from small acquisitions, large acquisitions and may be recent or old.

22) What is your assessment of the incremental costs and benefits of disclosing quantitative and qualitative information about the agreements underpinning material intangible items in (a) the period of the acquisition and (b) any changes to those agreements for several years post-acquisition? Please explain.

ValueKnowledge response: I suggest no change to current disclosure requirements. Greater qualitative and quantitative information about the underlying agreements may be useful to users of financial statements, but it may also be trade secrets and information that parties to those agreements would prefer to remain confidential for competitive and business reasons. Additionally, depending on demonstrated and expected rate of renewal and other factors, the contractual terms of agreements underlying the identified intangible asset value may have little relevance to the fair value measurement.

23) Are there other changes (deletions and/or additions) to the current disclosure requirements for goodwill or intangible items that the Board should consider? Please be as specific as possible and explain why.

ValueKnowledge response: N/A. I am usually not the primary person completing the disclosures, so I am not in a position to answer this question.

24) Under current GAAP, to what extent does noncomparability in the accounting for goodwill and certain recognized intangible assets between PBEs and private business entities and not-for-profit entities reduce the usefulness of financial reporting information? Please explain your response.

ValueKnowledge response: I suggest that PBEs and private business entities and not-for-profit entities adhere to the same standards. The continued emergence of “two GAAPs” will signal that accounting standards are not as important at some companies compared to others. The emergence of Update 2014-18 is detrimental to accounting in general.

25) Please describe the implications on costs and benefits of providing PBEs with an option on how to account for goodwill and intangible assets and the option for the method and frequency of impairment testing (described previously in Sections 1 and 2).
ValueKnowledge response: While I recognize that accounting for business combinations requires judgment, I encourage the FASB to retain a single standard among PBEs to reduce complexity and increase comparability company to company.

26) To what extent does noncomparability in the accounting for goodwill and certain recognized intangible assets between PBEs reporting under GAAP and PBEs reporting under IFRS reduce the usefulness of financial reporting information? Please explain your response.

ValueKnowledge response: In valuations, we use information from comparable companies to develop market multiples, observe industry capital structures and industry performance measurements. The more the PBEs diverge in their accounting, the more adjustments we must make to restore comparability. Equity analysts complete similar analyses as valuation specialists. Noncomparability in the accounting for goodwill would complicate valuation analysis and increase costs. Additionally, it may create a class system of accounting procedures, with non-PBEs’ accounting being deficient.

27) Please indicate the sources of comparability that are most important to you regarding goodwill and intangible assets. Please select all that apply and explain why comparability is not important to you in certain cases.
   a. Comparability among all entities reporting under GAAP (one requirement for PBEs, private business entities, and not-for-profit entities)
   b. Comparability among all PBEs reporting under GAAP
   c. Comparability among all private business entities and all not-for-profit entities reporting under GAAP
   d. Comparability among all PBEs reporting under GAAP and PBEs reporting under IFRS.

ValueKnowledge response: A, Comparability among all entities reporting under GAAP, would be most helpful for financial statement users, including valuation specialists.

28) Do you have any comments related to the Other Topics for Consideration Section or other general comments?

ValueKnowledge response: We have informally surveyed our clients that are PBEs for whom we have performed valuations that would be affected by the outcome of the issues raised in this ITC. The responses were enthusiastic and approximately evenly divided between maintaining the status quo and, alternatively, going toward US tax style of combining all the intangibles together and amortizing them over a pre-established period (in US tax law it is 15 years). The results of our survey have been considered in our comments. We learned from the survey that there is a variety of views on the topic, many strongly held, so I wish you wisdom in considering the pros and cons of revisions to existing guidance.
29) Would you be interested and able to participate in the roundtable?

ValueKnowledge response: Yes.

We appreciate the opportunity to submit this letter with Responses to the Invitation to Comment regarding Identifiable Intangible Assets and Subsequent Accounting for Goodwill Released November 19, 2018. Please contact Jim Krillenberger at 630-601-7126 or JAK@VKnow.com with any comments or questions.

Sincerely,

ValueKnowledge LLC
By: James A. Krillenberger, CFA, ASA