October 14, 2019

Technical Director, Financial Accounting Standards Board

File Reference No. 2019-720

Re: Invitation to Comment Identifiable Intangible Assets and Subsequent Accounting for Goodwill

The California Society of CPA’s (“CalCPA”) Accounting Principles and Assurance Services Committee (the “Committee”) is the senior technical committee of CalCPA. CalCPA has approximately 43,500 members. The Committee consists of 51 members, of whom 45 percent are from local or regional firms, 32 percent are from large multi-office CPA firms, 12 percent are sole practitioners in public practice, 6 percent are in academia and 5 percent are in international firms. Members of the Committee are with CPA firms serving a large number of public and nonpublic business entities, as well as many non-business entities such as not-for-profits, pension plans and governmental organizations.

We are happy to provide our response regarding the matters raised in the Invitation to Comment (ITC), Identifiable Intangible Assets and Subsequent Accounting for Goodwill. First, we want to highlight that the focus of our Committee is first and foremost on enabling high-quality financial reporting by companies of information that would be meaningful and relevant to users of the financial statements. With that stated, we also believe it is important to reduce the burden faced by the preparers to the extent possible without measurable reduction in the quality of financial information provided. Our discussions and replies to the questions in the ITC were driven by these general considerations.

Overall, our Committee did not reach a consensus on the key matter of whether goodwill should be amortized or continue to remain subject to impairment-only assessments. However, a majority of the committee members recommend retaining the existing model. This is based in part on the notion that the existing model is seen as providing relevant information to the users of the financial statements. It is also partially based on the fact that many entities have not yet adopted the most recent ASU affecting goodwill, ASU 2017-04. It would be odd to change altogether the accounting for goodwill and make obsolete pending changes to the existing model before most entities have even had a chance to adopt them and re-evaluate their experiences as relates to goodwill accounting.

Those members who prefer to retain the existing model are largely affiliated with auditor and user communities. Those members of the Committee affiliated with the preparer community would largely support transitioning to an amortization model.

If the amortization model is adopted, all Committee members expressed a preference for use of a meaningful (vs. default) amortization period, whether based on weighted average
useful lives of other identifiable asset(s) acquired, synergies, or other factors. Many of the Committee members would also advocate a cap on the goodwill amortization period.

Most of the Committee members also suggested to not make changes to the definition of intangible assets recognized in a business combination. The existing intangible assets model is seen as working and not creating significant challenges for entities; thus, there does not appear to be a significant need to change it. Some of the members supported updating the model to limit recognition to those assets meeting the asset definition in FASB Concept Statement No. 6.

Finally, all Committee members supported retaining the existing PCC alternative model for private and nonprofit entities.

Our detailed replies to the ITC are included in the Appendix.

We thank you for the opportunity to comment on these matters. We would be glad to discuss our opinions with you further should you have any questions or require additional information.

Sincerely,

Nancy A. Rix, Chair
Accounting Principles and Assurance Services Committee
California Society of Certified Public Accountants
APPENDIX

Invitation to Comment (ITC), Identifiable Intangible Assets and Subsequent Accounting for Goodwill

Replies to Questions

Section 1: Whether to Change the Subsequent Accounting for Goodwill

1. What is goodwill, or in your experience what does goodwill mainly represent?

   Goodwill may subsume multiple factors, such as synergies between the acquired business and the acquirer’s business; workforce; the value of future growth, and other. In certain industries in the modern technological world, we believe goodwill often reflects expectation about the acquired entity’s growth rate. However, in other industries it may be more closely associated with the acquired workforce, or components of technology (including some that are not separately recognized under the existing accounting rules). Additionally, to some members, goodwill is firmly attributed and associated with the acquired business (and any business within the acquiring entity integrated with the acquired business). Goodwill is seen as a wasting asset that requires ongoing efforts to maintain its value. To other members, goodwill becomes part of the value of the acquiring business, and is a non-wasting asset in that the combined entity generally expects ongoing growth and increase in value. Yet to others, it is simply a result of a calculation that includes consideration transferred and the value of various assets and liabilities acquired, akin to a “dangling debit”. The Committee observes that goodwill means different things to different people, and within different businesses. Depending on the preferred viewpoint and circumstances of the acquisition, it may be difficult to establish a consensus regarding goodwill accounting, or even a model that would not result in ongoing criticisms within members of the accounting community.

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.

   Although we did not reach a consensus, many members of our Committee, in particular those representing user and auditor communities, do believe that the current goodwill impairment model does provide sufficient benefits (in the form of information to the users) that justifies the associated costs. These members believe information about presence or absence of goodwill impairment helps inform users about performance of the entity (or reporting units within the entity) in comparison to the peers or to management expectations, and/or the impact on performance of various economic factors.
On the other hand, other committee members, generally those on the preparer side, emphasize that such information is costly to prepare and difficult to interpret, and for a number of reasons may not reflect performance of the specific acquired business where goodwill originated. As a result, the information provided may not be truly meaningful to users. Consequently, to these members, the benefit is limited and likely not justified by the costs.

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.**

Again, no consensus was reached. The majority of the members of the Committee who believe the current model provides sufficient benefits justifying the costs would not support transition to an amortization model for public companies. Those members who do not believe the current model provides relevant information would prefer transition to a model with amortization (with periodic impairment assessments).

In addition, CalCPA represents many constituents that are smaller private or non-profit entities. Many of these entities already amortize goodwill today under the Private Company Counsel (PCC) allowed alternative. Those members representing these constituents, regardless of whether they support impairment or amortization model for public entities, support retaining the amortization alternative for private and non-profit entities.

Some committee members prefer granting all entities a choice of an accounting policy to amortize or assess impairments on goodwill. Such policy would need to be clearly disclosed in the entity’s financial statements. Other members would not be opposed to an immediate write-off of acquired goodwill, as in their experience, any method of attributing goodwill charges to the income statement (i.e. amortization or impairment) may not produce information for the users that is particularly meaningful.

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

9. 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).

If the Board decides to have public companies amortize goodwill, most members of the Committee indicated they would be opposed to using a default period, as it would not provide meaningful information to the users, and would simply represent a charge most users will back out and ignore. The Committee members generally indicated they would prefer to have entities establish a meaningful amortization period. Such period could be based on alternative (f), i.e. weighted-average useful lives of identifiable asset(s) acquired; alternative (g), i.e. management’s reasonable estimate; or perhaps alternative (d), i.e. justification of a period other than a default period. Other alternative amortization periods may also be possible.

Most members also indicated they would prefer a cap on the period. A cap could be expressed in a form of a number of years (e.g., 10-20), or qualitatively (e.g., the longest of the periods over which other identifiable assets of the acquired business are amortized, the acquired workforce is expected to turn, etc.).

In addition, those members representing the entities eligible to use the PCC amortization alternative support retaining this alternative.

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.

Our members indicated their views on amortization vs. impairment do not depend on the amortization method and/or period. Amortization vs. impairment is the initial key judgment in accounting for goodwill; in the minds of the proponents of the impairment only approach, losing its benefits cannot be mitigated by the selection of the amortization method or period.

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.

Most members believe that if goodwill is amortized, charges based on an amortization period other than a default would provide decision-useful information to the investors, and such benefits would justify the related costs, for public entities. This is because amortization based on a default period would not result in a meaningful charge to the income statement for many of these entities, and investors would simply be expected to ignore what could be one of the larger amounts reported in that income statement.
Our members do support retaining the current default-period amortization model alternative for private and non-profit entities.

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.

Although it is still too early to tell as most entities have not yet adopted ASU 2017-04, we do not anticipate significant reductions in costs of goodwill impairment testing for most entities. This is because most entities do not proceed to Step 2 of the goodwill impairment test, as they are able to conclude goodwill is not impaired. For these entities, the cost of impairment testing could actually increase upon transition. This is because Step 1 will be used to measure goodwill impairment and generate a charge for the income statement, vs. serve as a threshold before the entity proceeds to Step 2. As a result, both management and auditors will need to put more precision into the quality of estimates and judgments underlying the information used in Step 1. Additionally, once an initial impairment is recorded, there will be no “cushion” left, and testing goodwill for impairment in the future quarterly and annual periods could become even more difficult and costly.

We do not believe the adoption of ASU 2017-04 will reduce the usefulness of financial reporting information. Today, users derive most benefit from the fact goodwill impairment has (or has not) occurred, as well as from its relative size compared to the carrying amount of goodwill or of the reporting unit. However, today’s concept of measuring impairment based on a hypothetical purchase price allocation is not intuitive to users, as all other amounts in this calculation are not reflected in the financial statements. One could argue that the amounts derived under the ASU 2017-04 approach may be more meaningful as they would directly reflect by how much the carrying value of the reporting unit may exceed its fair value.

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.

We do not believe ASU 2011-08 had a universal cost-reducing effect on entities. Some entities were able to benefit from its application, eliminating calculations required in Step 1. Many other entities found that performing a qualitative screen, and especially the level of support and documentation required to justify what may otherwise seem like obvious conclusions, was
excessive and would not justify the effort. While some of these entities elected to bypass the qualitative screen as a result, with arguably no impact on cost, other entities who went down the path of a qualitative screen found the cost they incurred is likely higher than Step 1 cost would have been.

We do not believe the adoption of ASU 2011-08 reduced the usefulness of financial reporting information, as it would arguably not impact the ultimate amounts reported by the entities.

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.**

Most members of the committee oppose removing the requirement for annual testing if the impairment-only model is retained. Our perception is that there is sufficient risk involved in carrying goodwill on the balance sheet as a non-amortizing asset, such that annual testing is justified.

In fact, although simplifications and improvements are always welcome, a majority of our committee members did not believe that at this time, there was a strong need to further change the current goodwill model.

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.**

Our Committee members strongly oppose the option to test goodwill for impairment at the entity level. However, we are not opposed to testing at levels other than the reporting unit level, as the reporting unit level is primarily an accounting convention created specifically for purposes of goodwill impairment testing.

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

Most of the members of the Committee do not believe significant changes in the existing accounting model for goodwill impairment are warranted at this time (or if warranted, would include transition to the amortization model). However, our Committee members are not opposed to implementing additional simplifications.

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.**
Section 2: Whether to Modify the Recognition of Intangible Assets in a Business Combination

13. Please describe what, if any, *cost savings* would be achieved if certain recognized intangible assets (for example, non-compete 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.

   While valuations of intangible assets may become simpler, it is likely that at least high-level estimates of the values of customer-related intangibles would still be performed, e.g. to determine contributory charges affecting valuation of other intangibles such as technology, or to validate the overall resulting goodwill amounts. After the initial acquisition accounting is completed, savings will be achieved from lack of need to record amortization of the eliminated intangible assets. However, usually preparing and processing such journal entries does not represent a significant cost to entities.

14. Please describe what, if any, *decision-useful information* would be lost if certain recognized intangible assets (for example, non-compete 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.

   Most of our members represent auditor community, and as such, we do not
perform performance analyses on these identified intangible assets. With that said, we do not support changing the definition of intangible assets and subsuming them into goodwill. We believe the existing definitions are well understood and consistently applied in practice by public companies. As a result, we do not believe there is a significant need to implement a change for the sake of a change.

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

We believe there are well accepted measurement techniques and practices in the valuation industry that make measurement of these intangible assets no less reliable than other intangibles.

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.**

We note that entities could dispose of various intangibles, including customer contracts and customer relations, outside the context of the business acquisition from which they originated. For example, an entity can sell and assign some but not all of its existing customer contracts if it chooses to divest a portion of an existing business. Such divestiture may not necessarily include a proportionate amount of goodwill. For example, divesting a high-growth portion of a business will likely include more goodwill than divesting a stable or shrinking portion of a business. Additionally, goodwill as currently defined may subsume other components. For example, in-process development of cloud-based internal-use software does not meet the definition of either technology or in-process research and development intangible assets, and in our experience may be included in goodwill. Disposing of a portion of the business together with the associated customer contracts may or may not involve any subsumed in-process internal-use software development. Finally, it is possible to sell and assign a single customer contract, which, as a single asset, will likely not meet the current definition of a business. Based on these examples, subsuming customer contract and similar intangibles into goodwill may not always produce meaningful results.

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.

Our Committee predominantly supports Approach 4. However, some of the Committee members support Approach 2, specifically, redefining intangible assets so they meet the definition of an asset in the FASB Concepts Statement No. 6. If goodwill is amortized, other committee members would support extending the PCC alternative to all entities.

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.

We believe practice will encounter certain operational challenges, as changes to the existing valuation practices will be required. As noted in our reply to question 13 above, there are relations and interconnections between various intangible assets and goodwill which are measured and leveraged under the existing valuation practices. If certain intangibles are no longer recognized, changes in such practices will be required. However, absent practice, it is difficult to foresee the exact extent of challenges that may arise.

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.

The Committee agrees that subsuming substantial intangible assets into goodwill would necessitate its amortization.

Section 3: Whether to Add or Change Disclosures about Goodwill and Intangible 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?

We are not clear as to what the intended trigger for disclosure would be. Entities are currently required to conduct impairment testing at least annually, and most of the testing does not result in impairment being recorded. If the suggestion is to require disclosure of additional information about any entity’s annual (or more frequent) impairment testing, the Committee would be opposed to this notion, because this in our opinion would be unnecessarily burdensome and as
a result would most likely evolve into boilerplate language that will not provide any practical value to any users. If the suggestion is to require disclosure of circumstances when an entity initiates Step 2 testing, Step 2 will no longer be performed with the adoption of ASU 2017-04.

21. **What other, operable ideas about new or enhanced disclosures would you suggest the Board consider related to goodwill?**

   Additional disclosures related to goodwill could include some or all of the following: (a) whether the entity conducted Step 1 (comparing fair values of the reporting units to the book values) or limited its test to Step 0 (qualitative assessment); and (b) whether a 10-20% adverse change in a relevant metric (e.g. reporting unit sales, foreign exchange rates, number of customers, etc.) would result in goodwill impairment, and the magnitude of such potential impairment.

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.**

   We do not support the notion of disclosing such information about the agreements underpinning material intangibles. We believe it would be unnecessarily burdensome for entities to track, accumulate, evaluate and compile information requiring disclosure. We also do not anticipate significant benefits to users of the financial statements, as such information will most likely be at a very high level (if quantitative) or boilerplate (if qualitative). There will also be a significant level of incremental effort required to audit such information if disclosed in the financial statements.

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.**

   We do not believe other changes to disclosures related to goodwill and other intangibles are required at this time.

### Section 4: Comparability and Scope

24. **Under current GAAP, to what extent does non-comparability 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.**

   We do not believe the lack of comparability between public and private/non-
profit entities has a significant effect on the usefulness of financial reporting information. There are many other sources of non-comparability between such entities, including different levels of overhead required to maintain compliance with public company regulations, different investor expectations, differences in financing structures, valuation of common stock and stock compensation charges, etc. Consequently, different accounting models for intangibles is merely one of the factors that affect such comparability.

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).

While several committee members believe such option would be useful, most members do not support this notion. Understanding the information reported in the financial statements would require understanding which option the entity has elected. As a result, financial analysis will become more manual and unnecessarily burdensome. Comparability between peer public companies will also be affected.

26. To what extent does non-comparability 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.

We support aligning US GAAP and IFRS approaches as much as practical. This is because there are many entities that are required for various reasons to maintain two sets of books, both US GAAP and IFRS. For these entities, conducting two different sets of records for goodwill is challenging. These challenges would be further exacerbated if in one set of books goodwill is amortized, and in the other one, only tested for impairment. We do welcome the issuance and adoption of ASU 2017-04 which brings US GAAP goodwill model closer to the IFRS.

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.
We believe the most relevant sources of comparability include comparability among all public entities reporting under US GAAP (answer b.); and comparability between entities reporting under US GAAP and IFRS (answer d.). Our reasons are described in the answers to some of the questions above.

**Other Topics for Consideration**

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

The Committee has no further observations on this topic.

**Next Steps**

**29. Would you be interested and able to participate in the roundtable?**

The Committee is happy to delegate a representative to the roundtable.