August 23, 2013

Ms. Susan M. Cosper  
Technical Director  
Financial Accounting Standards Board  
401 Merritt 7  
PO Box 5116  
Norwalk, CT 06856-5116  

File Reference No. PCC-13-01A

Dear Ms. Cosper:

McGladrey LLP appreciates the opportunity to comment on the Proposed Accounting Standards Update, Business Combinations (Topic 805), Accounting for Identifiable Intangible Assets in a Business Combination, a proposal of the Private Company Council (the “proposed Update”). Overall, we support the FASB’s efforts to provide an alternative for private companies in accounting for business combinations that allows for the separate recognition of only those identifiable intangible assets that arise from noncancelable contractual rights or from other legal rights, regardless of whether those assets are transferable or separable. The current model to separately account for all identifiable intangible assets is costly to private companies both in the initial year of the business combination and in subsequent year’s impairment evaluations. Estimating the fair value of all identifiable intangible assets often requires companies to incur the cost of using third party valuation specialists due to the significance of the intangible assets to the financial statements, even though all of these identifiable intangible assets may not be all that relevant to financial statement users. We believe the proposed Update will reduce overall costs and complexity for private companies that adopt this alternative compared with existing guidance and still result in users of private company financial statements receiving information that is decision-useful. Our responses to certain of the “Questions for Respondents” on which specific comment is sought and comments and suggestions on other matters in the proposed Update are included below for your consideration.

Comments on Certain Questions for Respondents

**Question 1: Please describe the entity or individual responding to this request.**

McGladrey LLP is a national CPA firm that serves hundreds of public companies and thousands of private companies in a variety of industries. We focus primarily on serving middle market companies and public sector entities.

**Question 2: Should any types of entities be excluded from the scope of this proposed Update? Should any types of transactions or accounts be excluded, or are there any types of transactions or accounts that should be included in the scope?**

We believe the scope of this proposed Update as it relates to types of transactions or accounts is appropriate. Refer to our response to Questions 3 and 15 for further discussion on the types of entities that should be included in the scope.
Question 3: Should the Board expand the scope of the accounting alternative to other entities, such as publicly traded companies or not-for-profit entities? If the scope is expanded to other entities, what changes, if any, should the Board consider for the recognition, measurement, and disclosure of identifiable intangible assets acquired in a business combination? If the scope is expanded to public companies or not-for-profit entities, should the accounting alternative continue to be elective?

We believe the Board should consider expanding the scope of the accounting alternative to include not-for-profit entities. By their very nature, not-for-profit entities may have even greater cost burdens obtaining valuations of identifiable intangible assets than other private entities and the identified intangible assets are arguably less relevant to the users of their financial statements.

The question of whether the scope of all accounting alternatives proposed by the PCC should apply to entities other than private entities will be a threshold question for every PCC proposal. In making this determination, we believe the Board must consider the information needs of the users of non-private company financial statements and whether the proposed alternative will result in these users having the necessary decision-useful information. Further to this, the Board should consider that these users generally can’t get further information from management (like private company users) and that these users will often be evaluating multiple companies. As a consequence of evaluating multiple companies, there may be difficulty from a comparability standpoint if one entity elects the alternative while another chooses not to elect the alternative.

As it relates to this particular issue, just by its very nature there is a lack of comparability due to the fact that two otherwise identical companies would have different financial presentations if one had expanded organically and the other expanded through acquisitions. Ultimately, we believe that further research should be done by the Board with the users of non-private company financial statements to gather further information on their needs and how they evaluate the current lack of comparability in order to make this assessment. If it is determined that these users do not consider all intangible assets that are reported on the balance sheet and adjust for intangible asset amortization and impairment charges when analyzing the entities’ financial statements, then we believe there would be support for expanding the scope of this accounting alternative to include public companies.

Question 4: Would the proposed amendments reduce overall costs and complexity compared with existing guidance? If not, please explain why.

We believe the proposed amendments will reduce complexity as some of the identifiable intangible assets that would no longer need to be separately recognized are those that often are very subjective and the most complex to value, such as customer relationships. We also believe that the proposed amendments will reduce costs, but it is unclear to us how significant those cost reductions will be. In many cases, private companies will still be required to utilize third party valuation specialists in order to determine the fair value of identified intangible assets arising from other legal rights that will continue to be recognized separately. In those situations, we’d still expect costs overall will be reduced as less work will be required of the third party valuation specialist, but it is unclear as to how significant these cost reductions will be.

Question 5: Do you agree that the accounting alternative for the recognition and measurement of intangible assets acquired in a business combination 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?

Our experience is that intangible asset impairment charges and amortization are often ignored by private company financial statement users (often predominantly lenders or engaged owners) as they utilize EBITDA or other metrics that exclude the effects of intangible asset impairment and amortization when evaluating the company. Quite often financial ratios are computed based on
tangible net worth and therefore exclude the impact of the intangible assets reflected on the balance sheet. As a result, we agree that the accounting alternative for the recognition and measurement of intangible assets acquired in a business combination would provide relevant and decision-useful information to users of private company financial statements.

**Question 6:** Do you agree that for contractual intangible assets, recognition and measurement should be limited to the noncancelable term of the contract? If so, do you agree with the proposed definition of a noncancelable contractual term? Do you agree that market participant expectations about the potential renewal or cancellation of the contract should not be factored into the measurement? Do you foresee any increase in cost and complexity or other difficulties in applying this alternative recognition and measurement principle? If yes, would additional implementation guidance address those difficulties?

We agree the recognition and measurement of contractual intangible assets should be limited to the noncancelable term of the contract. Further, we believe that market participant expectations about the potential renewal or cancellation of the contract should not be factored into the measurement as this will reduce complexity and the level of judgment involved in determining the value of these intangible assets.

In regard to the proposed definition of a noncancelable contractual term, we believe that it should be modified to clarify that contracts with terms that are not cancelable would also meet the definition of a noncancelable contractual term as follows (additions are underlined):

“805-20-25-31 In the preceding paragraph, a noncancelable contractual term is the portion of a contract that is either not cancelable or cancelable only under any of the following circumstances:"

We expect that the application of this alternative recognition and measurement principle will result in decreased costs and complexity since entities will only be required to value the estimated cash flows during the defined noncancelable contractual term without considering renewals or extensions and the more difficult to value non-contractual intangible assets (e.g., customer relationships, research and development assets) will no longer be separately recognized.

**Question 7:** Do you agree that intangible assets arising from other legal rights should continue to be measured at fair value considering all market participant expectations, consistent with Topic 820? If not, what accounting alternative for measurement do you recommend?

If the proposal is going to continue to require intangible assets arising from other legal rights to be accounted for separately, we agree that they should continue to be measured at fair value considering all market participant expectations. We would however question whether the cost of determining the fair value of these types of intangible assets is justified by the benefits being obtained by the users of the financial statements. Under the existing guidance, there is a lack of comparability due to the fact that two otherwise identical companies would have significantly different financial presentations if one had expanded organically and the other expanded through acquisitions (the former would have the intangible assets recorded at capitalized costs and the latter at fair value). In addition, in the case of long-lived assets that are difficult to value, the amount reflected on the balance sheet after several years of amortization could potentially be significantly different from its current fair value. Ultimately, we believe that further research should be done by the Board with the users of non-private company financial statements to gather further information on their needs and how they evaluate the current diversity in their use of the financial statements. If it is determined that these users do not make adjustments for intangible assets that are not at fair value and/or adjust for intangible asset amortization and impairment charges when analyzing the entities’ financial statements, then we believe that would support no longer accounting for these types of intangible assets separately.
**Question 8:** Do you agree that an entity should disclose the nature of identifiable intangible assets that are not recognized separately as a result of applying the amendments in this proposed Update? If not, please explain why.

We agree that an entity should disclose the nature of identifiable intangible assets that are not recognized separately as a result of applying the amendments in this proposed Update. We believe this information may be useful to private company financial statement users from a qualitative standpoint in situations in which they want to have further discussions with management about a particular identifiable intangible asset that is no longer separately recognized. While in some cases this may result in additional costs for private companies in identifying these intangible assets, we believe in most cases these costs would not be significant as companies would generally identify these intangible assets as part of their due diligence procedures prior to acquiring another entity.

**Question 9:** For identifiable intangible assets that are recognized separately as a result of applying the amendments in this proposed Update, do you agree that the amendments should not require any other additional recurring disclosures and that entities should be required to comply with disclosure requirements in relevant Topics, as applicable (for example, Topic 350, Intangibles—Goodwill and Other, and Topic 805)? If not, what additional disclosures should be required and please explain why.

We agree the amendments should not require any other additional recurring disclosures and that entities should be required to comply with disclosure requirements in other applicable relevant topics, for identifiable intangible assets that are recognized separately as a result of applying the amendments in this proposed Update.

**Question 10:** Do you agree that the proposed Update should be applied on a prospective basis? Should retrospective application be permitted?

We agree the proposed Update should be applied on a prospective basis. We don't believe retrospective application should be permitted due to concerns about the treatment of any intangible assets that were impaired prior to the effective date that would have been recorded as goodwill under the proposed Update if they were no longer required to be separately recognized.

**Question 11:** When should the alternative accounting method be effective? Should early application be permitted?

We believe the alternative accounting method should be effective immediately and entities should be allowed to adopt the guidance for all financial statements that have not yet been made available for issuance. This would be similar to the transition guidance on goodwill impairment testing in ASU 2011-08 which was in part as follows... “Earlier application also is permitted for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if the entity’s financial statements for the most recent annual or interim period have not yet been issued or, for nonpublic entities, have not yet been made available for issuance.”

**Question 12:** For preparers and auditors, how much effort would be needed to implement and audit the proposed amendments?

From an audit standpoint, we don’t expect that significant effort would be needed to audit the proposed amendments. However, the level of effort will vary depending on an entity’s specific facts and circumstances and whether further guidance is included in the final Update to address certain of the issues mentioned throughout this letter in our responses.
**Question 14:** If an entity elects the accounting alternative in this proposed Update, should that entity also be required to apply the PCC’s proposed accounting alternative for the subsequent measurement of goodwill (in Topic 350)? Alternatively, if an entity elects the accounting alternative in Topic 350 for goodwill, should that entity also be required to adopt the accounting alternative in this proposed Update? (No decisions have been reached by the Board and the PCC about this question.)

We believe if an entity wants to apply either accounting alternative they should be required to apply both accounting alternatives. There would be a number of complexities added to the model if entities were just allowed to adopt one of the accounting alternatives and we believe those complexities would add unnecessary costs. For example, if an entity was allowed to only adopt the accounting alternative in Topic 805, this would result in a larger amount of goodwill being recorded which would be subject to the existing guidance on goodwill impairment. Several issues would arise that we believe would need to be addressed in the guidance including: 1. As part of Step 2 of the goodwill impairment test, should an entity be required to value the identifiable intangible assets that were not separately recognized as part of the acquisition method accounting due to election of the accounting alternative in Topic 805?; and 2. Why is it appropriate for no amortization to be recorded for those identifiable intangible assets that otherwise would be amortized but are not because they were not separately recognized as a result of adopting the accounting alternative in Topic 805?

**Question 15:** The scope of this proposed Update 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, the Board 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. The Board 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 proposed Update. The Board 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 U.S. GAAP financial statements to be made publicly available on a periodic basis pursuant to a legal or regulatory requirement.

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

The question regarding the definition of a public business entity is a key question from a scoping standpoint that will be relevant for all PCC proposals. As the Board subsequently issued the proposed guidance referred to in this question as currently being deliberated, Proposed Accounting Standards Update, Definition of a Public Business Entity, An amendment to the Master Glossary, on August 7, 2013 with comments due by September 20, 2013, we will address this issue as part of our comment letter on that proposed Update.
Other Comments and Suggestions

Application of the Accounting Alternative to Typical Identifiable Intangible Assets Acquired in a Business Combination (proposed ASC 805-20-55-60)

We believe proposed ASC 805-20-55-60 would be clearer if the term “…with noncancelable terms” was deleted from items b through i, as we believe it is redundant to the introduction which states (emphasis added):

“…The values of these identifiable intangible assets would be determined on the basis of the contract’s noncancelable terms.”

Alternatively, we believe the example in proposed ASC 805-20-55-60a would be clearer if the following change was made for consistency (addition is underlined):

“…a. Order backlog as evidenced by outstanding purchase orders with noncancelable terms”

Transition from a private entity to a public entity

A key question for all PCC proposals that exclude public companies from their scope will be how private entities should make the transition from an accounting standpoint to being a public entity if they adopted an alternative accounting treatment. We believe that the answer to this question could vary depending on the particular proposal. For example, if adoption of an accounting alternative would result in a significant difference in accounting treatment that would affect comparability to other public entities, we believe it may be appropriate to require the private entity transitioning to a public entity to recast its financial statements for prior periods to conform to other public entities. However, if adoption of an accounting alternative would not affect comparability to other public entities, we believe the private entity transitioning to a public entity should not be required to recast its financial statements for prior periods to conform to other public entities. We believe these entities should just be required to follow the accounting guidance applicable to public entities on a prospective basis as the costs of retrospectively applying the public company accounting guidance would not seem to exceed the benefits.

We believe that this particular proposed Update would be an example of one in which prospective application is appropriate. As previously indicated, under existing guidance there is already a lack of comparability between entities that grow organically and those that grow through acquisition. We believe the Board should address this issue as part of any final Updates that are issued on accounting alternatives.

We would be pleased to respond to any questions the FASB or its staff may have concerning our comments. Please direct any questions to Rick Day (563.888.4017) or Brian H. Marshall (203.312.9329).

Sincerely,

McGladrey LLP