Goodwill Amortization

Released February 2022

Background

Accounting for goodwill is a controversial topic and FASB has made and continues to consider making changes to make it less burdensome. The FASB Board discussed goodwill accounting as recently as November 17, 2021.

Goodwill is an intangible asset that arises from business combinations. For GAAP purposes it is not amortized but is instead tested for impairment.

Most of the pushback to the existing accounting is the cost of determining if the goodwill is impaired. The guidance regarding the recognition of goodwill is set forth in FASB Statement No. 141 issued in 2004 and FASB Statement No. 141R (FAS ASC 805 – Business Combinations) which became effective in 2009. FASB Statement No. 142 (FAS ASC 350 – Goodwill and Other), issued in June 2001, provided guidance on goodwill impairment. It required entities to test for goodwill impairment whenever a triggering event occurs and at least annually using a two-step process:

- Step One – Compare the estimated fair value of the reporting unit with its book value, including the goodwill acquired. If the fair value is greater than the carrying amount, then no impairment is deemed to exist. If the fair value of the reporting unit is less than its carrying amount, then the acquired goodwill is considered to be impaired and a Step Two test must be performed.

- Step Two – Determine the fair value of the assets and liabilities of the reporting unit as if it had been acquired on the measurement date. Compare the resulting goodwill to the carrying amount and if the Step Two goodwill is less, then recognize a loss equal to the shortfall.

Since 2001, FASB has worked to address concerns and issued several updates to ease the costs and burdens of accounting for goodwill including:

- In 2011, FASB allowed all entities to perform a qualitative test of impairment, often called a Step 0. Only if the qualitative test showed that is more likely than not that the fair value of the goodwill is less than its carrying amount, does an entity have to perform a step one, or failing step one, a step two test.[1]

- In 2017, FASB eliminated the Step Two test.[2]

In addition, FASB gave relief to private companies in connection with the Private Companies Alternative Accounting Project:

[1] Accounting Standards Update ("ASU") No. 2011-08*, Intangibles – Goodwill and Other (Topic 350) Testing Goodwill for Impairment*

[2] ASU 2017-04, Intangibles – *Goodwill and Other (Topic 350) Simplifying the Test for Goodwill Impairment*

- In 2014, FASB allowed entities other than public business entities and not-for-profit entities to amortize to goodwill on straight-line basis over 10 years, or less than 10 years if appropriate.[3]

- In 2014, it permitted entities other than public business entities and not-for-profit entities to limit the recognition of intangible assets to: 1) customer-related intangible assets that can be sold or licensed separately from the other assets of the acquired business and 2) noncompetition agreements.[4]

In 2019, it extended the use of the accounting contained in the 2014 ASUs to not-for-profit entities.[5]

Last year, it allowed private companies and not-for-profit entities to perform a goodwill impairment triggering event evaluation at the end of the reporting period instead of throughout the year.[6]

Recent Deliberations

In 2018, FASB invited public comments on accounting for goodwill. In July 2020, it began initial deliberations regarding making changes to the accounting based on the comments received. Deliberations included the use of amortization. The FASB Board's most recent discussion focused on an appropriate amortization methodology. Following is a quick summary of FASB's most recent board discussions:

- <u>November 17, 2021</u>
  "The Board discussed details of the goodwill amortization period, including an overall amortization period estimation principle, a possible list of factors, providing a cap and floor on the amortization period, and the reassessment of an estimated goodwill amortization period."

- <u>June 23, 2021</u>
  "The Board discussed potential changes to the existing goodwill amortization model," including unit of account, the frequency of testing, and the timing of impairment.

- <u>April 7, 2021</u>
  The Board discussed "1) subsuming certain identifiable intangible assets in a business combination into goodwill and 2) factors entities could consider when estimating the useful life of goodwill if they chose to deviate from the default period and how such factors might affect the specifics of a potential cap on the amortization period".

---

[3] ASU 2014-02, Intangibles – *Goodwill and Other (Topic 350) Accounting for Goodwill*
[4] ASU 2014-18, *Business Combinations (Topic 805) Accounting for Identifiable Intangible Assets in a Business Combination*
[5] ASU 2019-06, *Intangibles – Goodwill and Other (Topic 350), Business Combinations (Topic 805), and Not-for-Profit Entities (Topic 958) Extending the Private Company Alternatives on Goodwill and Certain Identifiable Intangible Assets to Not-for-Profit Entities*
[6] ASU 2021-03, Intangibles – *Goodwill and Other (Topic 350), Accounting Alternative for Evaluating Triggering Events*

We will continue to monitor developments, but as of now, it appears that the Board is seriously considering the use of an amortization model. The question is whether they will require amortization.

We note that this paper is not intended to be an exhaustive discussion of the existing GAAP.

For more information on business combinations, goodwill, and goodwill impairment testing please see:

- Credit Union Purchase Accounting
- Credit Union Merger FAQs
- Accounting for Bank Acquisitions
- Accounting for Goodwill Impairment for Credit Unions
- Credit Unions Purchasing Community Banks