Qualitative Goodwill Impairment Assessment

A Roadmap to Applying the Guidance in ASU 2011-08

May 2012

Contents

Preface

This publication[1] addresses considerations related to adopting and performing a qualitative assessment of goodwill impairment in accordance with ASU 2011-08.[2] Key topics discussed include:

- Establishing and documenting the facts that are relevant to reporting units and goodwill balances.
- Updating processes and related internal controls in response to the guidance in ASU 2011-08.
- Identifying reporting units that bypass step 0 and proceed to step 1 of the traditional two-step impairment analysis.
- Evaluating events and circumstances to support an assertion that it is not more likely than not (MLTN)[3] that the fair value of a reporting unit is less than its carrying amount.
- Documenting the conclusions reached in the qualitative assessment.

The publication is divided into four main sections:

- *Introduction* — An overview of key considerations related to the qualitative assessment of goodwill impairment introduced by ASU 2011-08.
- *Adoption Considerations* — A summary of questions to consider when adopting ASU 2011-08.
- *Documentation and Process Considerations* — A comprehensive description of five steps that entities may consider when adopting ASU 2011-08 and performing the new assessment.
- *Interim Assessment* — A description of considerations related to performing a qualitative goodwill impairment assessment at times other than the annual measurement date.

The following are two Deloitte resources on this topic that entities may find helpful:

- September 16, 2011, *Heads Up*, *FASB Finalizes Amendments on Goodwill Impairment Testing*.
- *FASB's New Qualitative Goodwill Impairment Assessment*.

[1] This publication does not preclude the need for an entity to exercise professional judgment on the basis of its specific facts and circumstances. Further, practices related to performing a qualitative assessment may change over time as entities adopt the amended guidance.

[2] FASB Accounting Standards Update No. 2011-08, *Testing Goodwill for Impairment*.

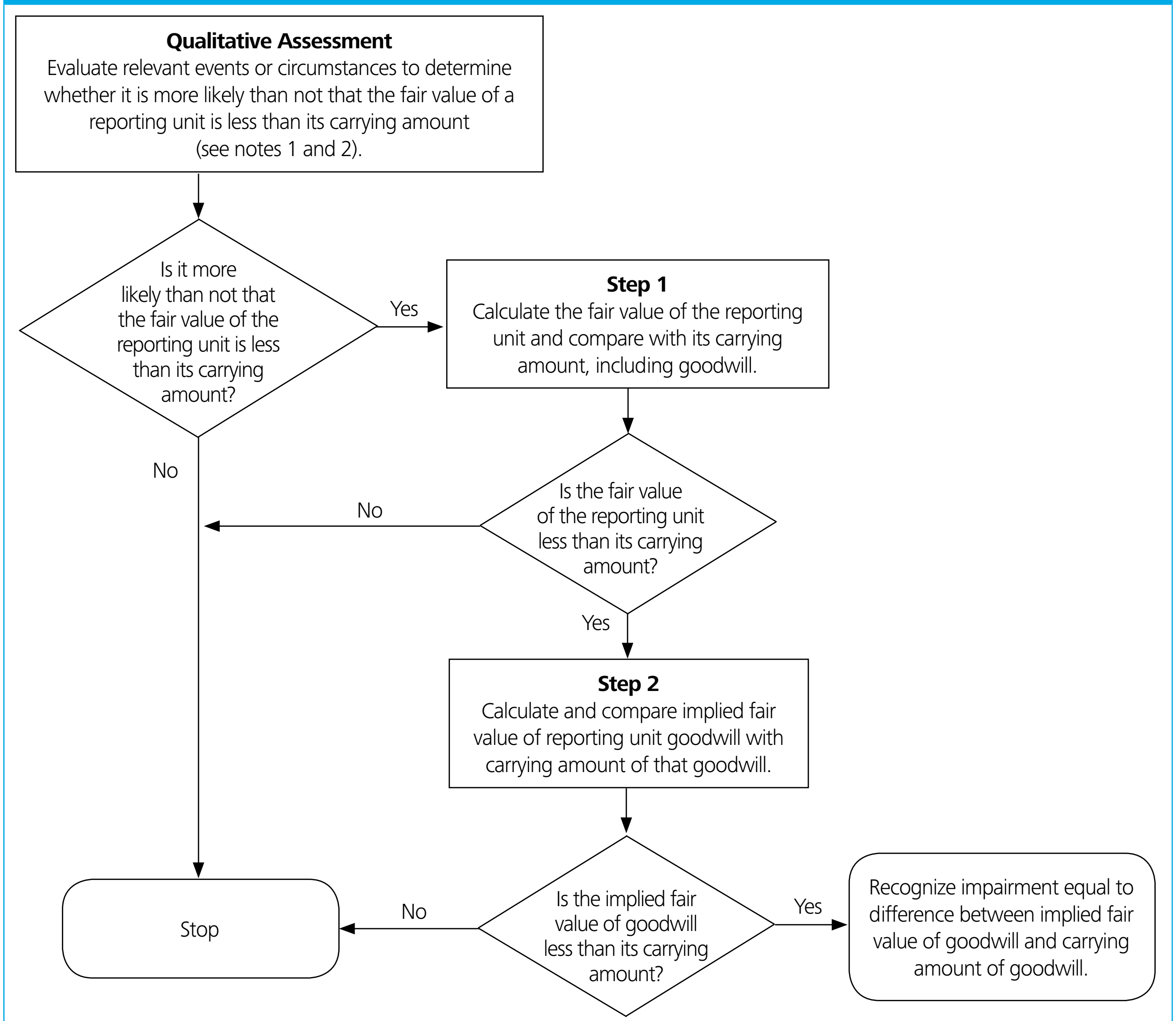
[3] A likelihood of more than 50 percent.

Introduction

In September 2011, the FASB issued ASU 2011-08, which gives entities the option of first performing a qualitative assessment to test goodwill for impairment on a reporting-unit-by-reporting-unit basis. If, after performing the qualitative assessment, an entity concludes that it is MLTN that the fair value of a reporting unit is less than its carrying amount, the entity would perform the two-step goodwill impairment test described in ASC 350.[4] However, if, after applying the qualitative assessment, the entity concludes that it is not MLTN that the fair value is less than the carrying amount, the two-step goodwill impairment test is not required.

The following flowchart (reprinted from ASC 350-20-55-25) illustrates the assessment process:

ASC 350-20-55-25



[4] For titles of *FASB Accounting Standards Codification* (ASC) references, see Deloitte's "Titles of Topics and Subtopics in the *FASB Accounting Standards Codification*."

ASC 350-20-55-25 (continued)

Notes:

1. An entity has the unconditional option to skip the qualitative assessment and proceed directly to performing Step 1, except in the circumstance where a reporting unit has a carrying amount that is zero or negative.
2. An entity having a reporting unit with a carrying amount that is zero or negative would proceed directly to Step 2 if it determines, as a result of performing its required qualitative assessment, that it is more likely than not that a goodwill impairment exists. To perform Step 2, an entity must calculate the fair value of a reporting unit.

Because the qualitative assessment (i.e., step 0) is optional, an entity may bypass it for any reporting unit in any period and begin its impairment analysis with the quantitative calculation in step 1. For example, if an entity has two reporting units, management may perform step 0 for one reporting unit and step 1 for the other reporting unit on the same measurement date. This option is unconditional in that entities may resume performing the qualitative assessment in any subsequent period. An entity that does not elect to use the qualitative analysis and proceeds directly to step 1 would not need to evaluate the qualitative factors in ASU 2011-08 as part of the annual impairment analysis. At the end of each reporting period following the annual assessment, an entity must evaluate whether the relevant events and circumstances described in ASC 350-20-35-3C have significantly changed, which may imply that the carrying amount of a reporting unit's goodwill is impaired.

Adoption Considerations

An entity may take different approaches to adopting the ASU depending on its facts and circumstances. Regardless of the entity's approach, the qualitative goodwill impairment assessment outlined in the ASU is highly subjective and will most likely require complex management estimates. Management should appropriately support any assertions made as part of this assessment.

Because of the subjectivity of the guidance in ASU 2011-08, it is important for entities to evaluate the ASU's requirements before preparing the qualitative assessment. Such evaluation may include consideration of the following questions:

- Has the goodwill impairment process been updated to take into account the changes resulting from the adoption of ASU 2011-08?
- What existing controls need to be modified, and what additional controls need to be designed, to address new risks of material misstatement related to the qualitative analysis? Given the recent issuance of ASU 2011-08, will these new controls be implemented in a timely manner?
- Is the most recent determination of fair value (i.e., the entity's "baseline" fair value) a good proxy for the current-period fair value?
- Will a third-party valuation specialist or another third-party firm be engaged to perform the qualitative analysis, or do internal personnel have the requisite skills to do so?
- Are there any events or circumstances suggesting that it is more appropriate to proceed to step 1 of the traditional two-step impairment analysis for one or more reporting units? For example:
    - Has a lot of time elapsed since the most recent valuation (e.g., was the carryforward option described in the superseded guidance in ASC 350-20-35-29 used for past measurement dates)?
    - Was the most recent valuation of a reporting unit derived in a manner other than in step 1 of the traditional two-step goodwill impairment analysis?
    - Did the most recent valuation of the reporting unit exceed the carrying amount of the reporting unit by a significant margin (i.e., cushion)?[5] If there is no, or an insignificant, margin between a reporting unit's carrying amount and the most recent fair value, it may be difficult to overcome this hurdle in a step 0 assessment.
    - Is there an MLTN expectation that a reporting unit or a significant portion of a reporting unit will be sold or otherwise disposed of?
    - Has the reporting unit significantly changed (e.g., acquisition or disposal) since the most recent valuation?
    - Are certain present or emerging factors so severe that it is unlikely that they can be overcome by other more favorable factors?
- What supporting documentation will be available to assist in the conclusion about each of the events and circumstances considered in the qualitative assessment?

[5] Calculated as the difference between the fair value and the carrying amount of the reporting unit, divided by the carrying amount of the reporting unit.

Documentation and Process Considerations

The following steps are intended to help entities adopt and apply the qualitative goodwill impairment assessment guidance in ASC 350-20:

- Step A: Compile and document relevant historical information about the entity and its reporting units.
- Step B: Consider updating processes and internal controls upon adopting ASU 2011-08.
- Step C: Identify reporting units for which an entity may proceed to step 1 of the traditional two-step impairment analysis.
- Step D: Assess events and circumstances to determine whether it is MLTN that the fair value of the reporting unit selected for the qualitative assessment is less than the carrying amount.
- Step E: Determine and document the results of the qualitative assessment performed to test goodwill for impairment.

Step A: Compile and Document Relevant Historical Information About the Entity and Its Reporting Units

As part of the goodwill impairment evaluation, an entity may find it helpful to accumulate relevant historical information related to goodwill and its reporting units. Such information may help an entity identify changes in reporting units, evaluate historical trends, determine the key business drivers, and consider the valuation techniques used to derive a reporting unit's fair value. The examples in this section are not intended to represent financial statement footnote disclosures but to help an entity document its impairment analysis.

Goodwill Related to Acquisitions

For each business combination, an entity should consider documenting the relevant information about the acquisition and related goodwill. Such information may include the following:

- The name of the acquired entity and the acquisition date.
- The amount of the purchase price recorded as goodwill on the acquisition date (including the rationale for allocating goodwill to one or more reporting units, if applicable).
- Any subsequent impairments or adjustments to goodwill, including the reason (i.e., description of facts and circumstances), amount written down, and any other relevant information.

Description of Reporting Units

ASC 350-20-20 defines a reporting unit[6] as "[t]he level of reporting at which goodwill is tested for impairment. A reporting unit is an operating segment or one level below an operating segment (also known as a component)." An entity should describe each reporting unit, identify its main business purpose, and determine the amount of goodwill allocated to it.

[6] This publication does not address how to determine reporting units. See ASC 350-20-35 for guidance on identifying reporting units.

Key Business Drivers

Describe and document the "key business drivers" for each reporting unit. A reporting unit's key business drivers can be defined as internal and external factors that are critical to the future growth of the reporting unit. Key business drivers are often evaluated as part of the annual budgeting process and can change year by year. It is therefore important for an entity to regularly consider its specific facts and circumstances in determining and evaluating key business drivers. Examples of key business drivers may include, but are not limited to, the following:

- Expected revenue and revenue growth rates.
- Expected operating expenses.
- Expected working capital requirements.
- Expected operating income and operating income growth rate.
- Expected operating margin.
- Expected depreciation and amortization.
- Expected capital expenditures.
- Economic and marketplace factors that are critical to the reporting unit.

Recorded Balances of Goodwill on the Measurement Date

An entity may summarize and document the following regarding the recorded goodwill carrying amount on the measurement date in its analysis:

- A summary, by reporting unit, of the carrying amount of goodwill on the current measurement date compared with the carrying amount on the prior-year measurement date. Consider presenting goodwill amounts in local currency, excluding the effects of foreign currency fluctuations.
- A description of any significant changes in the carrying amount from the prior year.

In addition, consider presenting a year-by-year comparison in a tabular format as follows:

	Carrying Amount of Goodwill			
Reporting Unit	Current-Year Measurement Date	Prior-Year Measurement Date	Difference ($)	Difference (%)
[Name of RU 1]	[$XXX,XXX]	[$XXX,XXX]	[$XXX,XXX]	[XX.X%]
[Name of RU 2]	[$XXX,XXX]	[$XXX,XXX]	[$XXX,XXX]	[XX.X%]
[Name of RU 3]	[$XXX,XXX]	[$XXX,XXX]	[$XXX,XXX]	[XX.X%]
Total	[$XXX,XXX]	[$XXX,XXX]	[$XXX,XXX]	[XX.X%]

Most Recent Valuation Technique

ASC 820 indicates that valuation techniques such as the market approach, income approach, cost approach, or a combination can be used to measure fair value. The entity should describe which valuation technique was used to calculate the most recent step 1 fair value amount. The description would include, but is not limited to, the following information:

- A summary, by reporting unit, of the step 1 fair value amounts and the technique used to derive each amount. Consider presenting such information in a tabular format as follows:

Reporting Unit	Fair Value Amount ($)	Most Recent Step 1 Fair Value Calculation Date	Fair Value Technique Used in Step 1 Calculation
[Name of RU 1]	[$XXX,XXX]	[MM/DD/YYYY]	[Income Approach/ Market Approach/Cost Approach/Combination]
[Name of RU 2]	[$XXX,XXX]	[MM/DD/YYYY]	
[Name of RU 3]	[$XXX,XXX]	[MM/DD/YYYY]	

- A description of the factors considered and the reason(s) for choosing the particular fair value technique over others.
- Documentation of the key valuation assumptions underlying the fair value calculation and a description of how these assumptions may have changed since the prior baseline measure of fair value was computed (including the impact that any such changes may have had on the fair value). Common valuation assumptions include, but are not limited to, the following:
  - Discount rate.
  - Corporate income tax rate.
  - Estimated near- and long-term growth rates.
  - Reporting-unit operating margins.
  - Valuation multiples.

Comparison of Baseline Fair Value With Carrying Amount

Summarize the information, by reporting unit, from the most recent measurement date by comparing the fair value and carrying amount. Consider presenting this information in a tabular format as follows:

	Most Recent Measurement Date			
Reporting Unit	**Carrying Amount**	**Fair Value**	**Excess/Deficit ($)**	**Excess/Deficit (%)**
[Name of RU 1]	[$XXX,XXX]	[$XXX,XXX]	[$XXX,XXX]	[XX.X%]
[Name of RU 2]	[$XXX,XXX]	[$XXX,XXX]	[$XXX,XXX]	[XX.X%]
[Name of RU 3]	[$XXX,XXX]	[$XXX,XXX]	[$XXX,XXX]	[XX.X%]

In addition, for each reporting unit, compare the carrying amounts on the current-year measurement date with the most recently calculated measure of fair value. Consider presenting this information in a tabular format as follows:

Reporting Unit	Carrying Amount of Reporting Unit on Current-Year Measurement Date	Fair Value of Reporting Unit on Most Recent Measurement Date	Excess/Deficit ($)	Excess/Deficit (%)
[Name of RU 1]	[$XXX,XXX]	[$XXX,XXX]	[$XXX,XXX]	[XX.X%]
[Name of RU 2]	[$XXX,XXX]	[$XXX,XXX]	[$XXX,XXX]	[XX.X%]
[Name of RU 3]	[$XXX,XXX]	[$XXX,XXX]	[$XXX,XXX]	[XX.X%]

Step B: Consider Updating Processes and Internal Controls Upon Adopting ASU 2011-08

Entities should consider the items below related to updating processes and controls when adopting ASU 2011-08.

- Who will perform, prepare, and review the qualitative analysis, and whether such personnel have the requisite skills to do so. For example, entities that previously engaged an external specialist to perform step 1, but that choose not to do so for step 0, should select the most appropriate internal personnel to gather and analyze data as well as to perform, document, and review the analysis. Further, if an entity's goodwill impairment test has historically been performed by a third-party valuation specialist, consider how this will affect the entity's consideration of who should be involved. An entity may need to engage external valuation specialists to help it (1) assess one or more relevant factors or (2) prepare sufficient documentation supporting the judgments the entity uses to make the assertion.

- How information about the events and circumstances needed to perform the qualitative impairment assessment will be gathered and evaluated (i.e., completeness of the assessment). For example, the entity should perform an evaluation to determine whether all relevant events and circumstances, including, but not limited to, those described in ASC 350-20-35-3C, are gathered with the help of personnel with an appropriate knowledge of the entity's operations (e.g., sales, operational personnel, business unit management, or legal and regulatory counsel).
- The type of review that will be performed on the step 0 assessment to determine the accuracy of the facts (i.e., accuracy of the assessment).
- When the fair value of a reporting unit will be calculated. For example, an entity may determine that a reporting unit's fair value will be calculated on a rotational basis. In such circumstances, the entity should determine how it would identify events and circumstances suggesting that it needs to calculate fair value at a time that is outside of the rotation.
- How qualitative events and circumstances will be evaluated on an interim basis. An entity should consider how the level and extent of documentation and evaluation necessary for interim assessments may differ from those for the entity's annual test.
- Establish and document the new or modified controls related to the assessment.

Step C: Identify Reporting Units for Which an Entity May Proceed to Step 1 of the Traditional Two-Step Impairment Analysis

When evaluating which reporting units are candidates for the qualitative assessment, an entity would consider the historical information accumulated in step A above and then determine whether any indicators suggest that the entity may need to calculate the fair value of the reporting unit under step 1 as of the current measurement date. These indicators may include, but are not limited to, the following:

- Contemplation of bankruptcy or concerns about the entity's ability to continue as a going concern.
- An MLTN expectation that a reporting unit, or a significant portion thereof, will be sold or otherwise disposed of.
- The planning or occurrence of recoverability testing for a reporting unit's significant asset group.
- Situations in which the fair value of a reporting unit must otherwise be calculated (e.g., the disposal of a portion of a reporting unit that constitutes a business or a reorganization of reporting units).
- Recording an impairment loss of a component of a reporting unit.
- Presence or emergence of negative factors that most likely cannot be overcome by other more favorable factors. Such negative factors include, but are not limited to, the following:
  - Declines in the macroeconomic environment or the industry in which the entity operates.
  - Decreases in revenues or cash flows.
  - Situations in which the reporting unit's performance is substantially less than the performance forecasted in the most recent valuation.
  - Significant volatility in the entity's operations.
- The fair value of a reporting unit has not recently been calculated.

Editor's Note: Entities should consider the duration between the most recent step 1 fair value calculation and the measurement date. Paragraph BC32 of ASU 2011-08 states, "The Board . . . acknowledged that the more time that elapses since an entity last calculated the fair value of a reporting unit, the more difficult it may be to make a conclusion based solely on a qualitative assessment of relevant events and circumstances."

- The most recent valuation of the reporting unit did not exceed its carrying amount by a significant margin.
- A significant change in the composition of the reporting unit's assets and liabilities (e.g., a significant acquisition or disposal) has occurred or is anticipated and this change makes the comparison to a prior-period fair value calculation less relevant.
- Cash flow projections are already being prepared to support other amounts in the financial statements. In

such cases, it may be more onerous to evaluate the qualitative factors in step 0 than to skip directly to the traditional two-step quantitative approach.

- A method other than the two-step goodwill impairment test discussed in ASC 350-20-35-4 through 35-19 was used to calculate the most recent valuation of a reporting unit (e.g., a newly acquired entity becomes its own reporting unit and the valuation is based on the purchase price).

Editor's Note: Although we believe the baseline quantitative fair value of the reporting unit that the entity uses to perform a step 0 qualitative assessment would generally be the value calculated in a prior step 1 analysis, ASU 2011-08 does not specifically address situations in which an entity has not previously performed a step 1 analysis. For example, there may be instances in which an entity makes an acquisition around the entity's annual goodwill impairment measurement date, the acquired business becomes a stand-alone reporting unit, and management relies on the recent valuation of the acquired business as an alternative to a step 1 analysis. In such circumstances, this **may** be an acceptable baseline to use for performing a step 0 qualitative assessment provided that the valuation performed on the acquisition date includes financial modeling effectively establishing that the entity has started with a "real measure" of fair value (i.e., management has relied on more than just the purchase price exchanged).

Step D: Assess Events and Circumstances to Determine Whether It Is MLTN That the Fair Value of the Reporting Unit Selected for the Qualitative Assessment Is Less Than the Carrying Amount

This section contains items and examples (not all-inclusive) for entities to consider in preparing the qualitative assessment for reporting units for which entities will perform step 0. These items are categorized under the events and circumstances identified in ASC 350-20-35-3C, because an entity's step 0 qualitative assessment is expected to at least address each of these events and circumstances, as applicable, for each reporting unit. In accordance with ASC 350-20-35-3F, management should factor additional events and circumstances into its qualitative assessment as necessary and should evaluate each event and circumstance, individually and together with other factors, to assess whether it is MLTN that the fair value of a reporting unit is less than its carrying amount.

An entity should consider whether the fair value calculated in a prior period actually remains a good proxy for the current fair value. The entity may support its conjecture by evaluating whether forecast scenarios used in the most recent fair value calculation continue to be reasonable in light of industry events and the entity's current circumstances. For example, such an assessment might include a quantitative analysis of the effects of market conditions, industry changes, and other factors on the cushion. Similarly, an entity might scrutinize the significant assumptions used in the most recent fair value calculation, such as projected revenue and revenue growth rates, to determine whether such assumptions remain appropriate in the current period.

To provide meaningful analysis of such trends, an entity might consider what quantitative analysis can be used to support its qualitative assertions. For example, an entity may document a year-by-year comparison for both budget and actual results to identify key trends in its financial performance. In addition, an entity may evaluate whether it continues to have the intent and ability to take any specific actions that were contemplated at the time of the most recent fair value calculation. For example, it may compare (1) any planned cost savings opportunities or other strategic plans that were contemplated in the prior forecasts with (2) actual results.

ASC 350-20-35-3C

In evaluating whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount, an entity shall assess relevant events and circumstances. Examples of such events and circumstances include the following:

a. Macroeconomic conditions such as a deterioration in general economic conditions, limitations on accessing capital, fluctuations in foreign exchange rates, or other developments in equity and credit markets

b. Industry and market considerations such as a deterioration in the environment in which an entity operates, an increased competitive environment, a decline in market-dependent multiples or metrics (consider in both absolute terms and relative to peers), a change in the market for an entity's products or services, or a regulatory or political development

ASC 350-20-35-3C (continued)

c. Cost factors such as increases in raw materials, labor, or other costs that have a negative effect on earnings and cash flows

d. Overall financial performance such as negative or declining cash flows or a decline in actual or planned revenue or earnings compared with actual and projected results of relevant prior periods

e. Other relevant entity-specific events such as changes in management, key personnel, strategy, or customers; contemplation of bankruptcy; or litigation

f. Events affecting a reporting unit such as a change in the composition or carrying amount of its net assets, a more-likely-than-not expectation of selling or disposing all, or a portion, of a reporting unit, the testing for recoverability of a significant asset group within a reporting unit, or recognition of a goodwill impairment loss in the financial statements of a subsidiary that is a component of a reporting unit

g. If applicable, a sustained decrease in share price (consider in both absolute terms and relative to peers).

Macroeconomic Conditions

In evaluating macroeconomic conditions, an entity should:

- Analyze the impact of the following macroeconomic conditions on the fair value drivers for the reporting unit:
  - "[D]eterioration in general economic conditions."
  - "[L]imitations on accessing capital."
  - "[F]luctuations in foreign exchange rates."
  - External economic data (e.g., U.S. Treasury rates, gross domestic product, movement and volatility in the stock market, and inflation).
  - "[O]ther developments in equity and credit markets."
- Consider the implications of attempting to access credit and whether it was successful, if applicable. Unsuccessful attempts to access capital markets may be indicative of a diminished fair value of the entity or individual reporting units.
- Consider whether fluctuations in foreign exchange rates affect currencies that mainly influence (1) sales prices for goods and services or (2) labor, material, and other costs of providing those goods or services. These fluctuations may negatively affect the fair value of a particular reporting unit within the entity.

Industry and Market Considerations

An entity should analyze the impact of the following industry and market factors on the fair value drivers of the reporting unit:

- "[A] deterioration in the environment in which the reporting unit operates."
- "[A]n increased competitive environment." For example, new competitors may take market share away from the entity, causing a decrease in revenue, which could result in a reduction in the reporting unit's fair value.
- "[A] decline in market-dependent valuation multiples or metrics, both in absolute terms and relative to peers." For example, a reporting unit that provides materials to the construction industry may anticipate a decline in revenue if demand for new housing starts to decline. If revenue is not replaced through sales to other customers or costs are not reduced proportionately, there may be a reduction in the fair value of the reporting unit.
- "[A] change in the market for a reporting unit's products or services." For example, a technological development or obsolescence of products or services, such as the change in formats of movies from DVDs to streaming, could result in a reduction in the fair value of the reporting unit.
- Regulatory developments. For example, the Dodd-Frank Wall Street Reform and Consumer Protection Act

may restrict entities from performing certain activities that would cause a reporting unit to incur additional costs of complying with this legislation. This may result in a decrease of net cash flows and a reduction in the fair value of the reporting unit.

- Political developments. For example, an increase in restrictions on offshore drilling may result in a reduction of revenue.

Further, an entity should determine the reporting unit's market share and evaluate how changes in market share and the overall market for the reporting unit's products and services may affect fair value (e.g., a stable or increasing market share may constitute evidence that the fair value of the reporting unit has increased or has not declined).

Moreover, an entity should consider whether the industry and market assumptions and judgments used for the qualitative assessment are consistent with those used for other purposes (e.g., whether assumptions and judgments supporting goodwill are inconsistent with those used to prepare budgets used for compensation purposes).

Cost Factors

With respect to cost factors, an entity should:

- Consider the impact of increases or decreases in raw materials, labor, and other cost factors that have an effect on earnings and cash flows and potentially the fair value of the reporting unit. Support the assessment by making quantitative analytical comparisons to measure the significance and extent of the impact of the cost factors. Such comparisons might include year-by-year results, budgeted versus actual results, and operating margins and capital expenditures versus prior-period and projected results.
- Develop a quantitative analysis to support how cost-cutting efforts initiated in the prior year have or have not affected current and projected margins.
- Consider whether the cost assumptions and judgments used for the qualitative assessment are consistent with those used for other purposes (e.g., whether the assumptions and judgments supporting goodwill are inconsistent with those used to prepare budgets used for compensation purposes).

Overall Financial Performance

When evaluating a reporting unit's overall financial performance, an entity should:

- Consider the impact of the reporting unit's overall financial performance metrics, which may include, but are not limited to, analysis of the following:
  - Cash flows into and out of the reporting unit(s) to determine whether the reporting unit is using financial resources more quickly than it is able to replace them with profits.
  - Increases or declines in "actual or planned revenue or earnings compared with actual and projected results for relevant prior periods."
  - Trends in historical revenue growth rates compared with those at peer companies.
  - Working capital needs, including whether the reporting unit's working capital requirements have changed and, if so, the reasons for the changes and a comparison of these explanations against the industry norms.
- Perform a retrospective review of significant assumptions and fair value drivers used in the most recent fair value calculation, including:
  - Comparing the actual recorded results for the current year with the forecasted results that were used in the most recently performed quantitative step 1 analysis.
  - Comparing updated current-period forecasts with the forecasts that were used in the most recently performed quantitative step 1 analysis.
- Consider the risk of failing to meet any debt covenants.
- Analyze key accounting ratios that may be useful to measuring the entity's business performance trends. These may include:
  - Liquidity ratios, which may indicate the entity's ability to meet short-term financial obligations.

- Efficiency ratios, which may indicate how well business assets are being used.
- Financial leverage ratios, which may indicate the sustainability of exposure to long-term debt.
- Gross profit margins, which indicate how much money is made after direct costs of sales have been taken into account.

Other Relevant Entity-Specific Events and Events Affecting a Reporting Unit

In addition, an entity should consider the impact of other events that may result in an increase or a decline in a reporting unit's fair value. Such events may include, but are not limited to, the following:

- Additions or losses of significant customers or dependence on major suppliers. For example, if any customers have discontinued, or are expected to discontinue, their use of the entity's products or services at any time, there could be a material adverse effect on the reporting unit's future results of operations. Further, supply chain shortages could create risk that orders placed by the reporting unit might not be fulfilled, thereby affecting the reporting unit's ability to meet its contractual commitments in an orderly manner.
- Effects of expiring patents, which could increase competition in the markets and therefore result in reduced revenues for the reporting unit.
- Technological conditions and influences.
- Products or industry trends.
- Future impacts of anticipated acquisitions/integrations, which could result in significantly abnormal returns and negative long-term performance in the post-acquisition integration period.
- Litigation.
- Changes in strategy.
- Expansion to new markets or withdrawal from certain markets.
- Adverse actions or assessments by regulators.
- Loss of key management or other personnel.
- A lack of product acceptance in the market.
- Commencement of liquidation sale.
- Natural disasters.

Further, ASC 350-20-35-3C(f) states that the likelihood and the significance of the following events (not all-inclusive) should be considered:

- "[C]hange in the composition or carrying amount of [a reporting unit's] net assets" (e.g., investments in equity method investments, joint ventures, and variable interest entities).
- "[A] more-likely-than-not expectation of selling or disposing of all, or a portion, of a reporting unit."
- "[T]he testing for recoverability of a significant asset group within a reporting unit."
- "[R]ecognition of a goodwill impairment loss in the financial statements of a subsidiary that is a component of a reporting unit."

Moreover, the entity should consider supplementing the qualitative discussion with a quantitative analysis or other underlying analysis, if appropriate, that measures the significance and extent of the impact of the events and circumstances described above.

A Sustained Decrease in Share Price

The entity should consider historical share price trends, which may include, but are not limited to, the following:

- Evaluation of stock price trends over a certain period (most notably, a sustained decrease in share price in both absolute terms and relative to peers).
- Comparisons with industry and peer companies.
- Comparisons with changes in the overall market.

It may prove beneficial to supplement the qualitative discussion with a quantitative analysis that measures the significance and extent of the impact of trends in, and comparisons of, the entity's share price. Such quantitative analyses may include sensitivity analyses that evaluate the potential impact of planned events on the entity's share price, comparisons to book value to understand any significant changes and determine the effect on the qualitative assessment, or evaluations of the market capitalization over time and compared with that of peer companies.

Deloitte Q&A — Assessing the Impact of a Decline in the Quoted Market Price of an Entity's Equity Securities

Question

If there is a decline in the quoted market price of an entity's equity securities and, thus, its market capitalization, is the entity required to test goodwill for impairment at the time of the decline?

Answer

Yes, if the underlying cause of the decline in quoted market price is determined to represent an event or change in circumstance that would MLTN reduce the fair value of the reporting unit below its carrying amount.

Under ASC 350-20-35-30, an entity must perform a goodwill impairment test "between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount." When the quoted market price of an entity's equity securities has declined, management should seek to identify the underlying cause of the decline to determine whether such an event or change in circumstance has occurred. ASC 350-20-35-3C lists a number of events and circumstances that may indicate that it is MLTN that a goodwill impairment exists, including "a sustained decrease in share price (consider in both absolute terms and relative to peers)." An entity's inability to identify an event or a change in circumstance that leads to a significant and sustained decline in the quoted market price of an entity's equity securities is expected to be infrequent.

Note that even if an entity's own securities have not declined significantly in value, management should still consider whether events and circumstances indicate that it is MLTN that the fair value of the reporting unit may be less than the carrying amount.

Step E: Determine and Document the Results of the Qualitative Assessment Performed to Test Goodwill for Impairment

The items in step D above, which are from ASC 350-20-35-3C, should be evaluated and documented for each reporting unit, since the assessment described in ASU 2011-08 is meant to be specific to the reporting unit.

An entity should document qualitative evidence of each key factor that is a driver of the reporting unit's fair value to support the discussion. If applicable, an entity should perform a quantitative analysis to support a qualitative discussion. Examples of quantitative support include the following:

- Financial modeling or sensitivity calculations.
- Opinions on or analyses of specific matters that require expertise of others.
- Projections of financial results.
- Analysis of prior-year projections compared with actual results.
- Economic and market data from sources, including:
    - Forrester Research Inc.
    - Hoovers.
    - Standard & Poor's.

  - Morningstar Inc.
  - Stocks, Bonds, Bills, and Inflation.
  - Cost of Capital Yearbook.
  - Web site of the Federal Reserve Statistical Release.

Key elements to be documented in the qualitative assessment should include the following:

- For each event and circumstance contemplated in the qualitative assessment, a conclusion about whether it represents positive, neutral, or adverse evidence that it is MLTN that the fair value of a reporting unit is less than its carrying amount. No one factor is meant to be a determinative event that triggers a step 1 calculation. Both the individual and the total impact of the events and circumstances should be evaluated.

ASC 350-20-35-3F

The examples included in paragraph 350-20-35-3C(a) through (g) are not all-inclusive, and an entity shall consider other relevant events and circumstances that affect the fair value or carrying amount of a reporting unit in determining whether to perform the first step of the goodwill impairment test. An entity shall consider the extent to which each of the adverse events and circumstances identified could affect the comparison of a reporting unit's fair value with its carrying amount. An entity should place more weight on the events and circumstances that most affect a reporting unit's fair value or the carrying amount of its net assets. An entity also should consider positive and mitigating events and circumstances that may affect its determination of whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If an entity has a recent fair value calculation for a reporting unit, it also should include as a factor in its consideration the difference between the fair value and the carrying amount in reaching its conclusion about whether to perform the first step of the goodwill impairment test.

- How heavily (e.g., low, medium, or high) each identified event or circumstance should be weighed in the overall assessment (i.e., an entity should place more weight on the events and circumstances that have the greatest effect on a reporting unit's fair value or the carrying amount of its net assets). A more robust analysis should be performed for those factors considered to be more significant to the overall analysis.

ASC 350-20-35-3G

An entity shall evaluate, on the basis of the weight of evidence, the significance of all identified events and circumstances in the context of determining whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. None of the individual examples of events and circumstances included in paragraph 350-20-35-3C(a) through (g) are intended to represent standalone events or circumstances that necessarily require an entity to perform the first step of the goodwill impairment test. Also, the existence of positive and mitigating events and circumstances is not intended to represent a rebuttable presumption that an entity should not perform the first step of the goodwill impairment test.

- For each reporting unit, an entity may consider using the template shown in the excerpt below to document the analysis related to each event or circumstance evaluated. The qualitative discussion may include quantitative analysis as described in step D above.

REPORTING UNIT #1

"a. Macroeconomic conditions such as a deterioration in general economic conditions, limitations on accessing capital, fluctuations in foreign exchange rates, or other developments in equity and credit markets."

[Include a qualitative discussion and analysis of this event or circumstance from ASC 350-20-35-3C for Reporting Unit 1. Conclude if the identified key factor had a positive, neutral or adverse impact on the comparison of fair value with carrying amount, and whether such impact was weighted as high, medium or low in accordance with ASC 350-20-35-3F and 35-3G, respectively. Based on the specific facts and circumstances of the key factor, consider quantifying the potential impact this has on the reporting unit's fair value. Consider summarizing the qualitative and quantitative discussion in a table shown below.]

	Adverse	Neutral	Positive	Relative Impact to Caparison FV and CA	Comments
Key Factor 1	X			High	[Add brief comments that help connect this summary to the qualitative discussion above.]
Key Factor 2		X		Medium	
Key Factor 3			X	Low	

"b. Industry and market considerations such as a deterioration in the environment in which an entity operates, an increased competitive environment, a decline in market-dependent multiples or metrics (consider in both absolute terms and relative to peers), a change in the market for an entity's products or services, or a regulatory or political development."

[Include a qualitative discussion and analysis of this event or circumstance from ASC 350-20-35-3C for Reporting Unit 1. Conclude if the identified key factor had a positive, neutral or adverse impact on the comparison of fair value with carrying amount, and whether such impact was weighted as high, medium or low in accordance with ASC 350-20-35-3F and 35-3G, respectively. Based on the specific facts and circumstances of the key factor, consider quantifying the potential impact this has on the reporting unit's fair value. Consider summarizing the qualitative and quantitative discussion in a table shown below.]

	Adverse	Neutral	Positive	Relative Impact to Caparison FV and CA	Comments
Key Factor 1	X			High	[Add brief comments that help connect this summary to the qualitative discussion above.]
Key Factor 2		X		Medium	
Key Factor 3			X		

Interim Assessment

ASC 350-20-35-30 states that "[g]oodwill of a reporting unit shall be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount." The examples of events and circumstances that an entity should consider are described in detail in step D. An entity must continue to evaluate whether events and circumstances have significantly changed since the annual impairment assessment.

As described in step B, after adopting ASU 2011-08, an entity would need to develop processes and implement controls. An entity should be prepared to document its assessment and conclusions reached in each reporting period. Although this analysis may not need to be as robust as the annual impairment assessment, an entity should have processes in place so that it can make the assertion that no significant changes have occurred since the annual assessment.

Deloitte Q&A — Timing of Goodwill Impairment Test

Question

When is an entity required to test goodwill for impairment?

Answer

The paragraphs below describe the circumstances in which goodwill must be tested for impairment in accordance with ASC 350-20.

Annually

ASC 350-20-35-28 notes that all goodwill must be tested annually for impairment. This paragraph further states that the "annual goodwill impairment test may be performed any time during the fiscal year provided the test is performed at the same time every year. Different reporting units may be tested for impairment at different times." Entities should evaluate their own facts and circumstances in assessing whether to establish different reporting dates for different reporting units. ASU 2011-08 does not change the requirement to test goodwill for impairment annually.

When Events or Circumstances Change

ASC 350-20-35-30 specifies that "[g]oodwill of a reporting unit shall be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. . . . Paragraph 350-20-35-3C(a) through (g) includes examples of such events and circumstances."

Annual testing for goodwill impairment notwithstanding, management must remain aware of events or circumstances (such as those listed in ASC 350-20-35-3C) that could indicate that a potential impairment has occurred between prescribed annual testing dates and must respond accordingly to such events or circumstances.

In evaluating whether it is MLTN that the fair value of a reporting unit will be less than its carrying amount, an entity should consider (1) the expected impact of the event or change in circumstances on the fair value of the reporting unit and (2) the amount by which fair value exceeds carrying value as of the date of the last impairment test. When the fair value of a reporting unit is only marginally higher than its carrying value, any expected decrease in the fair value of the reporting unit as a result of a subsequent event or change in circumstances should generally result in the conclusion that the entity needs to perform an impairment test.

Further, "if the carrying amount of a reporting unit is zero or negative, goodwill of that reporting unit shall be tested for impairment on an annual or interim basis if an event occurs or circumstances exist that indicate that it is more likely than not that a goodwill impairment exists." When assessing whether it is MLTN that goodwill is impaired, an entity should consider the events and circumstances listed in ASC 350-20-35-3C.

When a Portion of a Reporting Unit Is Disposed Of

ASC 350-20-35-51 through 35-57 state, in part:

> When a reporting unit is to be disposed of in its entirety, goodwill of that reporting unit shall be included in the carrying amount of the reporting unit in determining the gain or loss on disposal. When a portion of a reporting unit that constitutes a business . . . is to be disposed of, goodwill associated with that business shall be included in the carrying amount of the business in determining the gain or loss on disposal . . . based on the relative fair values of the business to be disposed of and the portion of the reporting unit that will be retained. . . . However, if the business to be disposed of was never integrated into the reporting unit after its acquisition and thus the benefits of the acquired goodwill were never realized by the rest of the reporting unit, the current carrying amount of that acquired goodwill shall be included in the carrying amount of the business to be disposed of. . . . When only a portion of goodwill is allocated to a business to be disposed of, the goodwill remaining in the portion of the reporting unit to be retained shall be tested for impairment in accordance with [ASC 350-20-35-4 through 35-19] using its adjusted carrying amount.