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On the Radar

Goodwill and Intangible Assets

Subsequent Accounting for Goodwill

ASC 350-20 addresses the accounting for goodwill after its initial recognition. While entities have been required to test goodwill for impairment for many years, the current goodwill accounting model has evolved significantly from the model that the FASB originally introduced in 2001. The FASB has issued numerous Accounting Standards Updates (ASUs) on this topic, which were generally intended to simplify or reduce the cost and complexity of performing goodwill impairment testing. As a result of those updates, ASC 350-20 now provides two accounting models used in the subsequent accounting for goodwill; the "general goodwill" model and the "goodwill accounting alternatives." The table below outlines the significant differences between the two accounting models.

Accounting for Goodwill Under ASC 350-20		
Significant Differences	**General Goodwill Model**	**Goodwill Accounting Alternatives**
Scope	Required for public business entities (PBEs) and may be applied by private companies and not-for-profit entities (NFPs)	Accounting policy elections available to private companies and NFPs
Amortization	Goodwill is not amortized	Goodwill is amortized over a useful life of 10 years or less

(Table continued)

Accounting for Goodwill Under ASC 350-20		
Significant Differences	**General Goodwill Model**	**Goodwill Accounting Alternatives**
Impairment testing	Goodwill is tested for impairment annually, or between annual tests if an impairment indicator exists (i.e., a triggering event)	Goodwill is tested for impairment only when an impairment indicator exists
Unit of account	Goodwill is tested for impairment at the reporting unit level	An entity elects to test goodwill at either the entity level or the reporting unit level
Monitoring for triggering events	An entity must monitor for goodwill triggering events throughout the reporting period	An entity may elect to only assess goodwill for triggering events at the end of each interim or annual reporting period

Considerations Before Adoption of the Goodwill Accounting Alternatives

While the FASB provided private companies and NFPs with the option of adopting a simplified goodwill accounting model, before electing any of the accounting alternatives, a private entity should consider whether it might become a PBE in the future (e.g., whether the entity may undertake an IPO or may be required to have its financial statements included in a registrant's filing under SEC Regulation S-X, Rule 3-05). Neither the FASB nor the SEC has provided relief or transition guidance for private companies that have elected the private-company accounting alternatives and later become PBEs; thus, private companies that might become PBEs should be cautious about electing them. Private companies that do apply the accounting alternatives and later become PBEs would need to retrospectively remove the effects of the accounting alternatives in any financial statements filed with, or furnished to, the SEC. The removal of such effects could become increasingly complex as more time passes.

Therefore, private companies that may later become PBEs should consider the potential future costs before electing any private-company alternatives. Specifically, paragraph BC32 of ASU 2021-03 notes:

> The Board acknowledges that reversing the accounting alternative would pose a challenge if a private company adopting the alternative wished to become a public business entity. To reverse the effects, an entity would need to go back to the date of adoption of the accounting alternative and evaluate (without hindsight) whether there were triggering events during the reporting period, including interim reporting periods, that would have resulted in a goodwill impairment and, if so, measure that impairment. However, those burdens are likely no more significant than would be the case for a private company that elected the alternative to amortize goodwill that subsequently elected to go public. The Board cautions entities that may eventually become public business entities to consider the potential future costs before electing this or any other alternative.

Subsequent Accounting for Intangible Assets

Once an intangible asset is recognized, an entity must determine the asset's estimated useful life. An intangible asset is either indefinite-lived or finite-lived on the basis of the intangible asset's expected useful life to the entity. The useful life of an intangible asset is considered indefinite if it is not limited by any legal, regulatory, contractual, competitive, economic, or other factors. The term "indefinite" does not mean infinite or indeterminate; it only means that the asset's life extends beyond the foreseeable horizon.

The subsequent accounting for an intangible asset varies considerably on the basis of whether the useful life of the asset to the entity is considered indefinite or finite. The table below highlights some key differences between finite-lived and indefinite-lived intangible assets.

	Finite-Lived Intangible Assets	Indefinite-Lived Intangible Assets
Characteristics	Expected useful life to the entity is limited.	No legal, regulatory, contractual, competitive, economic, or other factors limit the useful life to the entity.
Amortization period	Over the expected useful life to the entity.	Not applicable.
Amortization method	On the basis of the pattern in which the economic benefits are consumed or otherwise used up. If that pattern cannot be reliably determined, a straight-line amortization method should be used.	Not applicable.
Impairment testing	Tested for impairment in accordance with ASC 360 whenever events or circumstances indicate that the carrying amount of the asset (or asset group) may not be recoverable. An impairment loss is recognized if the carrying amount of the asset or asset group tested is not recoverable and its carrying amount exceeds its fair value (two-step test).	Tested for impairment in accordance with ASC 350 at least annually and more frequently if events or changes in circumstances indicate that the asset might be impaired. An entity may first perform the optional qualitative impairment assessment to determine whether it is more likely than not that the indefinite-lived intangible asset is impaired. If it is more likely than not that the asset is impaired, the entity would be required to perform a quantitative test by comparing the fair value of the asset with its carrying amount and recognizing an impairment loss for any excess. ASC 350-30-35-21 through 35-28 provide guidance on the unit of account to apply.

Selection of an Annual Testing Date for Goodwill and Indefinite-Lived Intangible Assets

The goodwill in each reporting unit, as well as each indefinite-lived intangible asset, must be tested for impairment at least annually. An entity may select any date throughout the year on which to perform its annual impairment test as long as this selection is applied consistently each year. An entity can elect different annual testing dates for different reporting units and different indefinite-lived intangible assets. However, we observe that entities often select the same date for all of their reporting units and indefinite-lived intangible assets.

When selecting an annual assessment date, entities should be mindful of quarterly reporting requirements and filing deadlines to ensure that they have enough time to complete the testing before the financial statements are issued. For this reason, entities often avoid choosing the end of an annual or quarterly reporting period. Public companies often select the first day of their fourth quarter as their annual testing date since (1) they will have the carrying amounts from the last day of the prior quarter available, (2) they have the entire quarter to perform the necessary valuation work, and (3) this timing is often aligned with the timing of the preparation of their budgets and forecasts for the next year. Another common date is the first day of the second month of the fourth quarter (i.e., November 1 for calendar-year-end companies) since that date may be even better aligned with preparation of budgets and forecasts and yet still give the entity enough time to complete testing before the financial statements are issued.

Changing the Date of the Annual Impairment Test

An entity is permitted to change its annual impairment testing date. An entity that wants to change its goodwill impairment testing date must evaluate the change as a change in accounting principle under ASC 250. Accordingly, the entity must (1) determine that the change is preferable, (2) ensure that no more than 12 months elapse between the tests, and (3) ensure that the change is not made with the intent of delaying or accelerating a goodwill impairment charge. By contrast, an entity's testing date for its indefinite-lived intangible assets is

not an accounting policy election. An entity that changes its annual impairment testing date for indefinite-lived intangible assets does not have to evaluate the change as a change in accounting principle under ASC 250. However, the entity should ensure that no more than one year elapses between tests.

While a voluntary change in accounting principle should be applied retrospectively, we have observed that entities typically apply a change in goodwill testing date prospectively rather than retrospectively because either (1) they determine that retrospective application would be impracticable on the basis of the guidance in ASC 250-10 or (2) the change does not have a material effect on the financial statements given the existing requirements in ASC 350-20 to assess goodwill for impairment between annual tests upon the occurrence of a triggering event.

An SEC registrant that voluntarily changes an accounting principle is generally required to include a preferability letter issued by its independent registered public accounting firm as Exhibit 18 to its first periodic report filed after the accounting change. However, in the case of a change in the goodwill assessment date, an SEC registrant is only required to obtain and file a preferability letter with the Commission when the registrant determines that a reported change in the date of the annual impairment test is material. However, even if a registrant determines that it is unnecessary to obtain and file a preferability letter related to a change in the annual impairment testing date because the change is immaterial, the staff would still expect the registrant to prominently disclose the change within the applicable filing (e.g., Form 10-K, Form 10-Q).

Market Capitalization Reconciliation

While not required to do so by ASC 350-20, a publicly traded entity often compares its market capitalization with the aggregate of the fair values of all of its reporting units when testing goodwill for impairment, because such a comparison can yield useful information about the reasonableness of the fair value measurements. Entities must use judgment when reviewing the comparison for factors that may indicate appropriate differences between the market capitalization and the aggregate sum of the fair value of the reporting units.

The SEC staff frequently refers to an entity's market capitalization when commenting on the entity's testing of goodwill for impairment. When an entity's book value is greater than its market capitalization, questions may be raised about whether goodwill should be tested for impairment or, if goodwill was tested, whether goodwill at one or more reporting units is impaired. Entities should be able to explain how having a greater book value than market capitalization affected their judgments regarding the testing of goodwill for impairment.

Early-Warning Disclosures

In addition to the requirements in ASC 275-10-50 to disclose certain risks in the financial statements, SEC Regulation S-K, Item 303(b)(2), requires registrants to discuss in MD&A a known uncertainty — specifically, to disclose the potential for a material impairment charge — in light of potential impairment triggers (i.e., whether the registrant should have provided early-warning disclosures about the possibility of an impairment charge in future periods to help financial statement users understand these risks and how they could potentially affect the financial statements). The SEC staff expects a registrant that has recorded, or is at risk for recording, an impairment charge to disclose the following:

- The adequacy and frequency of the registrant's impairment tests, including the date of its most recent test.
- The factors or indicators (or both) used by management to evaluate whether the carrying value of other long-lived assets may not be recoverable.
- The methods and assumptions used in the impairment tests, including how assumptions compare with recent operating performance, the amount of uncertainty associated with the assumptions, and the sensitivity of the estimate of the fair value of the assets to changes in the assumptions.
- The timing of the impairment, especially if events that could result in an impairment had occurred in periods before the registrant recorded the impairment.

- The types of events that could result in impairments.
- In the critical accounting estimates section of MD&A, the registrant's process for assessing impairments.
- The facts and circumstances that led to the impairments. A registrant should also consider disclosing in MD&A risks and uncertainties associated with the recoverability of assets in the periods before an impairment charge is recorded. For example, even if an impairment charge is not required, a reassessment of the useful life over which depreciation or amortization is being recognized may be appropriate.

In addition, the staff may use hindsight, after an impairment or charge is reported (e.g., a material impairment charge), to inquire why the registrant did not include any early-warning disclosures in prior periods leading up to the reporting of such impairment. Such disclosures alert investors to the underlying conditions and risks that the company faces before a material charge or decline in performance is reported.

Deloitte's Roadmap *Goodwill and Intangible Assets* provides Deloitte's insights into and interpretations of the guidance in ASC 350-20.

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