Grant Thornton

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Viewpoint

Impairment: Indefinite-lived intangibles and goodwill

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Introduction

Accounting for the impairment of goodwill and other indefinite-lived intangible assets can be challenging because it involves performing multiple steps, each one requiring an entity to exercise judgment. Those steps include

- Determining which unit of account to use in testing the intangible assets for impairment;
- Applying the various impairment models in U.S. GAAP, in the appropriate order, based on the types of assets reported on the entity's balance sheet; and
- Determining whether the assets are impaired and, if so, measuring the impairment.

Not only are the steps important, but an entity must perform them in a designated sequence, or it risks not recognizing an existing impairment or recognizing an inappropriate amount of impairment.

This publication summarizes the FASB's guidance on accounting for the impairment of goodwill under ASC 350-20, as well as the impairment of indefinite-lived intangible assets under ASC 350-30.

Under U.S. GAAP, an entity must generally assess indefinite-lived intangible assets, including goodwill, for impairment at least annually and then additionally on an interim basis if a "triggering event" occurs. A "triggering event" occurs when the entity determines that it is more likely than not that the carrying amount of an indefinite-lived intangible asset is less than its fair value or, in the case of goodwill, that the carrying amount of a reporting unit is less than its fair value. (The phrase "more likely than not" is generally understood to mean a likelihood of more than 50 percent.) Determining whether a triggering event occurs requires significant judgment, as does determining the fair value of an indefinite-lived intangible asset or, in the case of goodwill, a reporting unit for the purposes of measuring impairment. Although the guidance on recognizing the impairment of goodwill and the impairment of indefinite-lived intangible assets is in many ways similar, there are distinctions in U.S. GAAP, as described in this publication.

In recognizing that impairment testing can be costly and time consuming for entities, the FASB issued several Accounting Standards Updates (ASUs) to simplify the impairment testing process, including ASU 2017-04, which eliminates Step 2 of the goodwill impairment test. Those amendments apply to SEC public filers for years beginning after December 15, 2019 and to public entities that are not SEC filers for years beginning after December 15, 2020; for all other entities, the amendments apply for years beginning after December 15, 2021. This publication incorporates the guidance in ASU 2017-04 because we anticipate that most entities have already adopted these amendments. Entities that have not yet adopted these amendments may refer to ASC 350-20 for guidance on applying Step 2 of the goodwill impairment test.

This publication also discusses the amendments under ASU 2021-03, which allows nonpublic business entities to evaluate goodwill impairment triggering events at the end of a reporting period instead of during the reporting period. The amendments in ASU 2021-03 are effective on a prospective basis for fiscal years beginning after December 15, 2019.

This Viewpoint features direct citations from the FASB's Codification, insights gleaned by Grant Thornton professionals, and examples to illustrate different aspects of impairment testing. We will update this publication periodically to reflect new guidance and practice issues that develop in relation to impairment testing under ASC 350.

The following flowcharts provide a summary of the annual and interim impairment models under U.S. GAAP for indefinite-lived intangible assets and goodwill.

Figure 1: Impairment testing model for indefinite-lived intangible assets, including goodwill

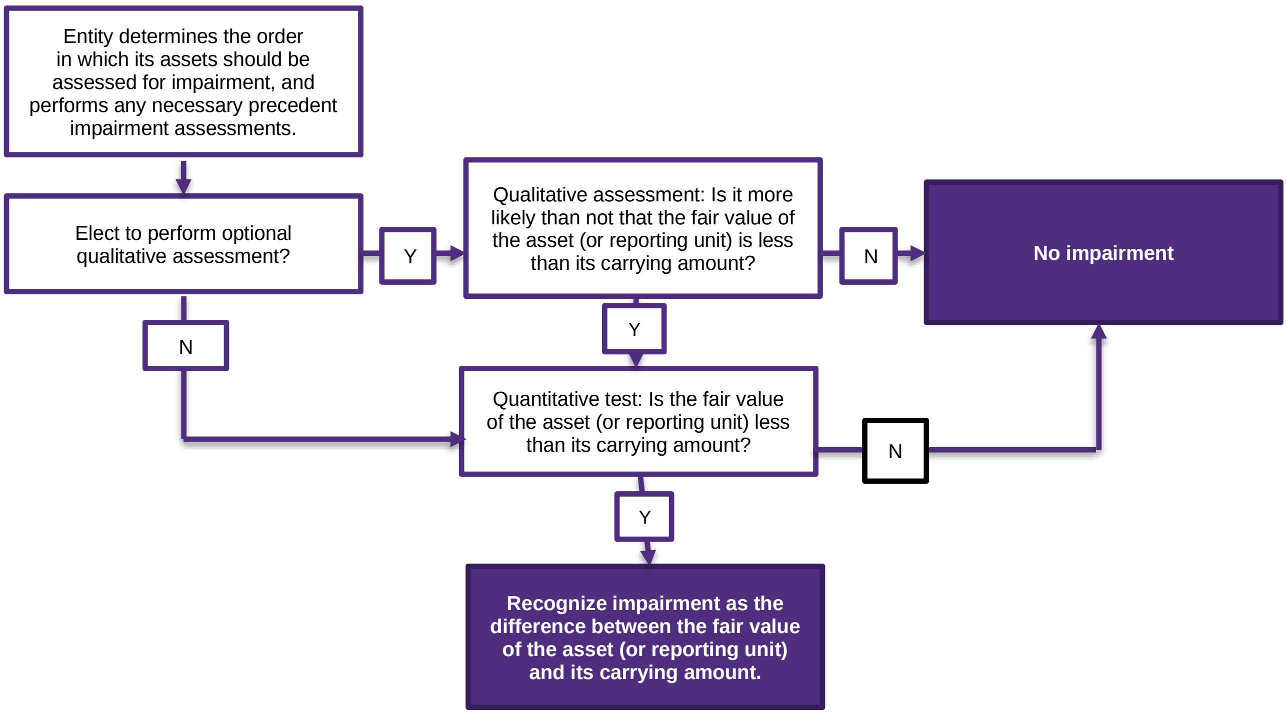
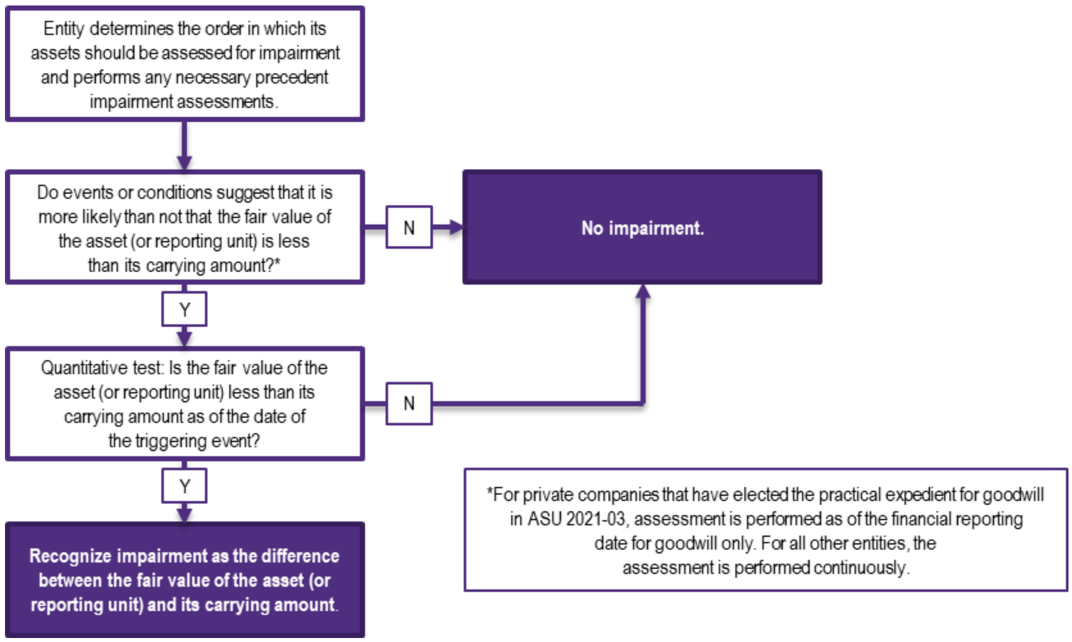


Figure 2: Interim impairment testing model for indefinite-lived intangible assets, including goodwill



1 Order of impairment testing

Under ASC 360, entities with tangible long-lived assets and intangible assets are required to evaluate those assets for impairment. Intangible assets with indefinite lives, including goodwill, are evaluated for impairment at least annually and then additionally in a subsequent interim period if an impairment triggering event occurs between annual tests. An impairment triggering event occurs when there are indicators that the fair value of an asset (or, in the case of goodwill, the reporting unit) may be below its carrying amount.

On the other hand, tangible long-lived assets and intangible definite-lived assets are tested for impairment only when a triggering event indicates that the asset's carrying amount may not be recovered. If this type of triggering event is identified for one class of assets, it might also indicate the identification of a similar triggering event for other classes of assets, requiring an entity to test multiple classes of assets for impairment simultaneously.

When testing multiple classes of assets for impairment, the order in which the assets are tested is important, because some assets are tested individually for impairment while others are tested as part of a group of assets. For instance, the model for testing goodwill impairment under ASC 350 compares the fair value of a reporting unit to its carrying amount, while the model in ASC 360 for certain tangible long-lived assets and finite-lived intangible assets calls for testing these assets for impairment as part of an asset group. Under ASC 360 an asset group may be comprised solely of an individual asset. The order of testing when evaluating goodwill and asset groups for impairment is important because the impairment assessment for both classes of assets depends on the carrying amount of the reporting unit or asset group. In turn, the carrying amount of the reporting unit or asset group depends on the individual assets within the group being appropriately adjusted for impairment before an entity can assess goodwill or an asset group for impairment. Overall, individual assets are tested before asset groups, and asset groups are tested before reporting units.

Because the goodwill impairment model in ASC 350-20 compares a reporting unit's fair value to its carrying amount, the impairment tests for other types of assets, such as inventory, long-lived assets, indefinite-lived intangible assets (except goodwill), and finite-lived intangible assets, should be completed first, with the carrying amount for those assets and asset groups adjusted for any impairment before conducting the goodwill impairment test, which should be performed last. If impairment testing is not performed in the appropriate order, the impairment testing results for assets tested earlier or later may not be appropriate. For instance, if impairments related to other classes of assets that are included within a reporting unit are not appropriately recognized, then the carrying value of the reporting unit used to measure goodwill impairment may be an inappropriately greater amount; the reporting unit's carrying value would be higher compared to its fair value because the other asset classes were not first reduced for impairment.

ASC 350-20-35-31

If goodwill and another asset (or asset group) of a reporting unit are tested for impairment at the same time, the other asset (or asset group) shall be tested for impairment before goodwill. For example, if a significant asset group is to be tested for impairment under the Impairment or Disposal of Long-Lived Assets Subsections of Subtopic 360-10 (thus potentially requiring a goodwill impairment test), the impairment test for the significant asset group would be performed before the goodwill impairment test. If the asset group was impaired, the impairment loss would be recognized prior to goodwill being tested for impairment.

ASC 350-20-35-32

This requirement applies to all assets that are tested for impairment, not just those included in the scope of the Impairment or Disposal of Long-Lived Assets Subsections of Subtopic 360-10.

According to the guidance in both ASC 350-20-35-31 and ASC 360-10-35-27, entities should evaluate for impairment assets that are held-for-use based on the unit of account in the following order:

1. *Individual assets* – First, an entity should individually test for impairment assets that must be tested under guidance other than ASC 360, excluding goodwill, as well as tangible long-lived assets tested individually under ASC 360. Those assets tested individually for impairment include indefinite-lived intangible assets, financial assets, deferred tax assets, servicing assets, long-lived assets held-for-sale, and inventory. (Note that in this publication, *indefinite-lived intangible assets* refers to indefinite-lived intangible assets other than goodwill.)

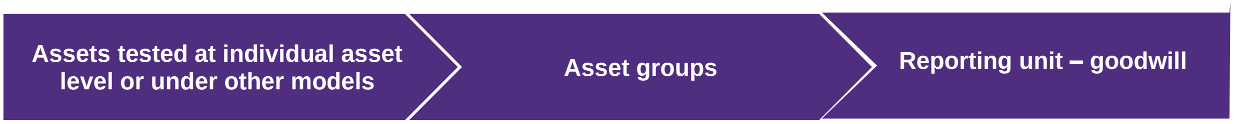
2. *Asset groups* – Next, an entity should test asset groups for impairment using the model in ASC 360, including long-lived assets held-for-use, definite-lived intangible assets, and right-of-use assets recognized under ASC 842.

3. *Reporting unit* – Finally, after an entity performs all other impairment tests, goodwill should be tested based on the reporting unit model in ASC 350.

Grant Thornton insight: Enterprise assets

An entity may also hold enterprise assets or corporate support assets, which are assets that support the revenue-generating activities of multiple asset groups. For example, a tangible long-lived asset such as a trade name that supports the revenue-generating activity of multiple asset groups should be included in a higher-level asset group containing all the asset groups that benefit from the individual trade name asset for the purposes of testing the trade name asset for impairment. In this scenario, the entity should test the trade name as part of the higher-level asset group, which includes all of the lower-level asset groups that use the trade name to generate their cash flows. The carrying value of enterprise assets that support more than one asset group should not be allocated to multiple asset groups. Rather, the lower-level asset groups that benefit from the use of the enterprise asset should be tested for impairment individually prior to testing the higher-level asset group that includes the enterprise asset.

Figure 3: Order of impairment testing



Example: Order of impairment testing

APG Corp. has the following assets:

- Inventory
- Receivables
- Property, plant, and equipment
- Finite-lived intangibles
- Indefinite-lived intangibles
- Financial assets
- Goodwill
- Deferred tax assets

APG Corp. determines that its property, plant, and equipment and its finite-lived intangibles are part of one asset group for the purposes of impairment testing. On October 31, 20X1, in connection with its required annual impairment assessment for its indefinite-lived intangibles and goodwill, APG Corp. determines that it has experienced a triggering event for those assets. APG Corp. further determines that the triggering event also indicates that certain of its definite-lived intangible assets and long-lived tangible assets may not be recoverable and should also be tested for impairment.

Based on the asset types held by APG Corp., the entity should test for impairment in this order: First, assets that are required to be tested for impairment individually; next, assets that are tested as asset groups; and, finally, goodwill. The order of the assets tested for impairment are as follows.

First: Individual assets	Second: Asset groups	Last: Reporting unit
Inventory	Property, plant & equipment	Goodwill
Receivables	Finite-lived intangibles	
Indefinite-lived intangibles		
Financial assets		
Deferred tax assets		

Assets that are tested individually under specific guidance (such as guidance on inventory or receivables), as well as indefinite-lived intangible assets subject to ASC 350-30, are tested for impairment first. Next are the assets that are part of an asset group under the guidance in ASC 360. Lastly, goodwill is tested for impairment. Any impairment adjustments resulting from testing the first and second groups of assets are recognized prior to determining the carrying amount of a reporting unit used for the purpose of testing goodwill under the guidance in ASC 350-20.

2 Impairment models for indefinite-lived intangible assets, other than goodwill

ASC 350 includes guidance on the impairment models that should be used for testing indefinite-lived intangible assets, including goodwill. Indefinite-lived intangible assets are tested for impairment using the guidance in ASC 350-30, while goodwill is tested for impairment using the guidance in ASC 350-20.

2.1 Identifying indefinite-lived intangible assets

Under ASC 350-30-35-4, the useful life of an asset is considered to be “indefinite” if no legal, regulatory, contractual, competitive, economic, or other factors limit the asset’s useful life. Examples of assets that may have indefinite lives include certain trade names, trademarks, and perpetual franchises.

An intangible asset has an indefinite life if its life extends beyond the foreseeable horizon, according to ASC 350-30-35-4. An entity does not need to establish that an intangible asset’s life is infinite for the asset to be considered indefinite-lived, but an intangible asset’s life is not necessarily indefinite if an entity cannot determine its life precisely. The accounting guidance in ASC 350-30-35-4 distinguishes between asset lives that are *indeterminant* and those that are *indefinite*. An entity should perform a detailed analysis of all relevant facts and circumstances when determining whether there is a limit on the useful life of an intangible asset or whether the asset’s life is indefinite.

ASC 350-30-35-4

If no legal, regulatory, contractual, competitive, economic, or other factors limit the useful life of an intangible asset to the reporting entity, the useful life of the asset shall be considered to be indefinite. The term indefinite does not mean the same as infinite or indeterminate. The useful life of an intangible asset is indefinite if that life extends beyond the foreseeable horizon—that is, there is no foreseeable limit on the period of time over which it is expected to contribute to the cash flows of the reporting entity. Such intangible assets might be airport route authorities, certain trademarks, and taxicab medallions.

The evaluation of whether intangible assets are indefinite-lived or have a finite life requires judgment based on individual facts and circumstances. ASC 350-30-55 includes examples that illustrate circumstances when an entity would determine that the acquired intangible assets are indefinite-lived.

Example 4 – Acquired Broadcast License Deemed to Have an Indefinite Life

ASC 350-30-55-12

An acquired broadcast license expires in five years. The broadcast license is renewable every 10 years if the entity provides at least an average level of service to its customers and complies with the applicable Federal Communications Commission (FCC) rules and policies and the FCC Communications Act of 1934. The license may be renewed indefinitely at little cost and was renewed twice prior to its recent acquisition. The acquiring entity intends to renew the license indefinitely, and evidence supports its ability to do so. Historically, there has been no compelling challenge to the license renewal. The technology used in broadcasting is not expected to be replaced by another technology any time in the foreseeable future. Therefore, the cash flows from that license are expected to continue indefinitely.

ASC 350-30-55-13

The broadcast license would be deemed to have an indefinite useful life because cash flows are expected to continue indefinitely. Therefore, the license would not be amortized until its useful life is deemed to be no longer indefinite. The license would be tested for impairment in accordance with paragraphs 350-30-35-18 through 35-20.

Example 6 – Acquired Airline Route

ASC 350-30-55-18

An acquired airline route authority from the United States to the United Kingdom expires in three years. The route authority may be renewed every five years, and the acquiring entity intends to comply with the applicable rules and regulations surrounding renewal. Route authority renewals are routinely granted at a minimal cost and have historically been renewed when the airline has complied with the applicable rules and regulations. The acquiring entity expects to provide service to the United Kingdom from its hub airports indefinitely and expects that the related supporting infrastructure (airport gates, slots, and terminal facility leases) will remain in place at those airports for as long as it has the route authority. An analysis of demand and cash flows supports those assumptions.

ASC 350-30-55-19

Because the facts and circumstances support the acquiring entity's ability to continue providing air service to the United Kingdom from its U.S. hub airports indefinitely, the intangible asset related to the route authority is considered to have an indefinite useful life. Therefore, the route authority would not be amortized until its useful life is deemed to be no longer indefinite and would be tested for impairment in accordance with paragraphs 350-30-35-18 through 35-20.

Example 8 – Acquired Trademark Determined to Have Reduced Cash Flows

ASC 350-30-55-24

A trademark that distinguished a leading consumer product was acquired 10 years ago. When it was acquired, the trademark was considered to have an indefinite useful life because the product was expected to generate cash flows indefinitely. During the annual impairment test of the intangible asset, the entity determines that unexpected competition has entered the market that will reduce future sales of the product. Management estimates that cash flows generated by that consumer product will be 20 percent less for the foreseeable future; however, management expects that the product will continue to generate cash flows indefinitely at those reduced amounts.

ASC 350-30-55-25

As a result of the projected decrease in future cash flows, the entity determines that the estimated fair value of the trademark is less than its carrying amount, and an impairment loss is recognized. Because it is still deemed to have an indefinite useful life, the trademark would continue to not be amortized and would continue to be tested for impairment in accordance with paragraphs 350-30-35-18 through 35-20.

The following examples from the Codification describe situations when an entity determines that the acquired intangible assets have a finite life.

Example 1 – Acquired Customer List

ASC 350-30-55-3

A direct-mail marketing entity acquired a customer list and expects that it will be able to derive benefit from the information on the acquired customer list for at least one year but for no more than three years.

ASC 350-30-55-4

The customer list would be amortized over 18 months, management's best estimate of its useful life, following the pattern in which the expected benefits will be consumed or otherwise used up. Although the acquiring entity may intend to add customer names and other information to the list in the future, the expected benefits of the acquired customer list relate only to the customers on that list at the date of acquisition (a closed-group notion). The customer list would be reviewed for impairment under the Impairment or Disposal of Long-Lived Assets Subsections of Subtopic 360-10.

Example 2 – Acquired Patent

ASC 350-30-55-6

An acquired patent expires in 15 years. The product protected by the patented technology is expected to be a source of cash flows for at least 15 years. The reporting entity has a commitment from a third party to purchase that patent in 5 years for 60 percent of the fair value of the patent at the date it was acquired, and the entity intends to sell the patent in 5 years.

ASC 350-30-55-7

The patent would be amortized over its five-year useful life to the reporting entity following the pattern in which the expected benefits will be consumed or otherwise used up. The amount to be amortized is 40 percent of the patent's fair value at the acquisition date (residual value is 60 percent). The patent would be reviewed for impairment under the Impairment or Disposal of Long-Lived Assets Subsections of Subtopic 360-10.

If an intangible asset's life is determined to be indefinite, that asset should not be amortized until its life is determined to be finite. An entity is required to evaluate in each reporting period whether the life of an intangible asset previously identified as indefinite is now finite. If the intangible asset is determined to have a finite life, the entity would need to test the intangible asset for impairment under the model for intangible assets with indefinite lives in ASC 350-30, comparing the fair value of the intangible asset to its carrying amount. After recognizing any impairment, the entity would then amortize the asset over its newly determined remaining useful life. Intangible assets that remain indefinite-lived would still be subject to the impairment testing guidance under ASC 350-30.

ASC 350-30-35-15

If an intangible asset is determined to have an indefinite useful life, it shall not be amortized until its useful life is determined to be no longer indefinite.

ASC 350-30-35-16

An entity shall evaluate the remaining useful life of an intangible asset that is not being amortized each reporting period to determine whether events and circumstances continue to support an indefinite useful life.

ASC 350-30-35-17

If an intangible asset that is not being amortized is subsequently determined to have a finite useful life, the asset shall be tested for impairment in accordance with paragraphs 350-30-35-18 through 35-19. That intangible asset shall then be amortized prospectively over its estimated remaining useful life and accounted for in the same manner as other intangible assets that are subject to amortization.

The following example in ASC 350-30-55 illustrates when an indefinite-lived intangible asset is no longer deemed to have an indefinite life (in other words, its useful life becomes finite).

Example 9 – Acquired Trademark No Longer Deemed to Have an Indefinite Life

ASC 350-30-55-27

A trademark for a line of automobiles was acquired several years ago in an acquisition of an automobile entity. The line of automobiles had been produced by the acquired entity for 35 years with numerous new models developed under the trademark. At the acquisition date, the acquiring entity expected to continue to produce that line of automobiles, and an analysis of various economic factors indicated there was no limit to the period of time the trademark would contribute to cash flows. Because cash flows were expected to continue indefinitely, the trademark was not amortized. Management recently decided to phase out production of that automobile line over the next four years.

ASC 350-30-55-28

Because the useful life of that acquired trademark is no longer deemed to be indefinite, the trademark would be tested for impairment in accordance with paragraphs 350-30-35-18 through 35-20. The carrying amount of the trademark after adjustment, if any, would then be amortized over its remaining four-year useful life following the pattern in which the expected benefits will be consumed or otherwise used up. Because the trademark will be subject to amortization, in the future it would be reviewed for impairment under the Impairment or Disposal of Long-Lived Assets Subsections of Subtopic 360-10.

2.2 Determining the unit of account for impairment testing

When performing an impairment test for indefinite-lived intangible assets, an entity generally tests those assets individually; however, the guidance in ASC 350-30-35-21 requires an entity to combine separately recorded indefinite-lived intangible assets into a single unit of account for impairment testing if the assets operate as a single asset and are inseparable from one another (for instance, separate trade name assets recognized in different countries for the same brand would most likely operate as a single asset and be inseparable from each other). Entities may need to use significant judgment based on the relevant facts and circumstances to determine whether the assets should be combined for purposes of impairment testing.

ASC 350-30-35-21

Separately recorded indefinite-lived intangible assets, whether acquired or internally developed, shall be combined into a single unit of accounting for purposes of testing impairment if they are operated as a single asset and, as such, are essentially inseparable from one another.

The guidance in ASC 350-30-35-23 discusses indicators that may assist entities in determining when an entity should combine two or more indefinite-lived intangible assets into a single unit of accounting for impairment testing, while ASC 350-30-35-24 discusses indicators for when it is inappropriate to combine such assets into a single unit of accounting.

ASC 350-30-35-23

Indicators that two or more indefinite-lived intangible assets shall be combined as a single unit of accounting for impairment testing purposes are as follows:

a. The intangible assets were purchased in order to construct or enhance a single asset (that is, they will be used together).

b. Had the intangible assets been acquired in the same acquisition they would have been recorded as one asset.

c. The intangible assets as a group represent the highest and best use of the assets (for example, they yield the highest price if sold as a group). This may be indicated if it is unlikely that a substantial portion of the assets would be sold separately or the sale of a substantial portion of the intangible assets individually would result in a significant reduction in the fair value of the remaining assets as a group.

d. The marketing or branding strategy provides evidence that the intangible assets are complementary, as that term is used in paragraph 805-20-55-18.

ASC 350-30-35-24

Indicators that two or more indefinite-lived intangible assets shall not be combined as a single unit of accounting for impairment testing purposes are as follows:

a. Each intangible asset generates cash flows independent of any other intangible asset (as would be the case for an intangible asset licensed to another entity for its exclusive use).

b. If sold, each intangible asset would likely be sold separately. A past practice of selling similar assets separately is evidence indicating that combining assets as a single unit of accounting may not be appropriate.

c. The entity has adopted or is considering a plan to dispose of one or more intangible assets separately.

d. The intangible assets are used exclusively by different asset groups (see the Impairment or Disposal of Long-Lived Assets Subsections of Subtopic 360-10).

e. The economic or other factors that might limit the useful economic life of one of the intangible assets would not similarly limit the useful economic lives of other intangible assets combined in the unit of accounting.

Grant Thornton insight: Additional considerations for combining indefinite-lived intangibles into one unit of account

In addition to the indicators presented in ASC 350-30-35-23 and 35-24, the unit of account for indefinite-lived intangible assets is restricted to only indefinite-lived intangible assets, and those assets cannot be combined with other assets, such as definite-lived intangible assets or goodwill. Also, when issuing stand-alone subsidiary financial statements, entities should not combine assets of other subsidiaries within the subsidiary’s stand-alone financial statements.

However, indefinite-lived intangible assets owned by different subsidiaries in a consolidated group that are presented in the separate financial statements of the subsidiaries should be combined into one unit of account for purposes of impairment testing at the consolidated entity level, if those assets operate as a single asset at the consolidated group level. As a result, the impairment loss reported in the consolidated financial statements may differ from the impairment recognized in the stand-alone financial statements of the subsidiaries.

The following examples from ASC 350-30-55 illustrate how an entity determines the unit of account to be used in impairment testing for indefinite-lived intangible assets.

Example 10 – Easements

ASC 350-30-55-30

Entity A is a distributor of natural gas. Entity A has two self-constructed pipelines, the Northern pipeline and the Southern pipeline. Each pipeline was constructed on land for which Entity A owns perpetual easements that Entity A evaluated under Topic 842 and determined do not meet the definition of a lease under that Topic (because those easements are perpetual and, therefore, do not convey the right to use the underlying land for a period of time). The Northern pipeline was constructed on 50 easements acquired in 50 separate transactions. The Southern pipeline was constructed on 100 separate easements that were acquired in a business combination and were recorded as a single asset. Although each pipeline functions independently of the other, they are contained in the same reporting unit. Operation of each pipeline is directed by a different manager. There are discrete, identifiable cash flows for each pipeline; thus, each pipeline and its related easements represent a separate asset group under the Impairment or Disposal of Long-Lived Assets Subsections of Subtopic 360-10. While Entity A has no current plans to sell or otherwise dispose of any of its easements, Entity A believes that if either pipeline was sold, it would most likely convey all rights under the easements with the related pipeline.

ASC 350-30-55-31

Based on an evaluation of the circumstances, Entity A would have two units of accounting for purposes of testing the easements for impairment—the collection of easements supporting the Northern pipeline and the collection of easements supporting the Southern pipeline. The 50 easements supporting the Northern pipeline represent a single unit of accounting as evidenced by the fact that they are collectively used together in a single asset group (see paragraphs 360-10-35-23 through 35-26), if acquired in a single transaction, they would have been recorded as one asset, and if sold, they would likely be sold as a group with the related pipeline. For the same reasons, the easements supporting the Southern pipeline would represent a single unit of accounting.

ASC 350-30-55-32

Because the collective land easements underlying the Northern and Southern pipelines generate cash flows independent of one another and are used exclusively by separate asset groups under the Impairment or Disposal of Long-Lived Assets Subsections of Subtopic 360-10, they should not be combined into a single unit of accounting.

Example 11 – Trade Name

ASC 350-30-55-34

Entity B purchases an international vacuum cleaner manufacturer, Entity A, which sells vacuums under a well-known trade name. The operations of Entity A are conducted through separate legal entities in three countries and each of those legal entities owns the registered trade name used in that country.

When the business combination was recorded, Entity B recorded three separate intangible trade name assets because separate financial statements are required to be prepared for each separate legal entity. There are separate identifiable cash flows for each country, and each country represents an asset group under the Impairment or Disposal of Long-Lived Assets Subsections of Subtopic 360-10. A single brand manager is responsible for the Entity A trade name, the value of which is expected to be recovered from the worldwide sales of Entity A’s products.

ASC 350-30-55-35

Based on an evaluation of the circumstances, three separately recorded trade name assets would be combined into a single unit of accounting for purposes of testing the acquired trade name for impairment. The three registered trade names were acquired in the same business combination and, absent the requirement to prepare separate financial statements for subsidiaries, would have been recorded as a single asset. The trade name is managed by a single brand manager. If sold, Entity C would most likely sell all three legally registered trade names as a single asset.

Example 12 – Brands

ASC 350-30-55-37

Entity Z manufactures and distributes cereals under two different brands, Brand A and Brand B. Both brands were acquired in the same business combination. Entity Z recorded two separate intangible assets representing Brand A and Brand B. Each brand represents a group of complementary indefinite-lived intangible assets including the trademark, the trade dress, and a recipe. Brand A has two underlying trade names for its Honey and Cinnamon cereals. The trade name and recipe of Cinnamon were internally generated subsequent to the acquisition of Brand A. Sales of Honey have decreased while sales of Cinnamon have increased over the past several years. Despite the decline in sales of Honey, the combined sales of Honey and Cinnamon have increased at the levels expected by management. Sales of Brand B also have increased at expected levels. There are discrete cash flows for Honey, Cinnamon, and Brand B, and each represents a separate asset group under the Impairment or Disposal of Long-Lived Assets Subsections of Subtopic 360-10. Both Honey and Cinnamon are managed by one brand manager. A separate brand manager is responsible for Brand B; however, there are some shared resources used by these groups, such as procurement. While Entity Z has no current plans to sell its brands or exit the cereal business, it believes if it ever did, it would exit the cereal business in its entirety.

ASC 350-30-55-38

Based on an evaluation of the circumstances, Entity Z would have two units of accounting for purposes of testing the acquired brands for impairment. Brand A’s purchased Honey and internally generated Cinnamon trademarks should be combined as a single unit of accounting for purposes of impairment testing. The intangible asset associated with the Cinnamon trademark is simply a variation of the previously acquired Brand A Honey trademark. Although they are associated with different asset groups, they are managed by a single brand manager. Entity Z would consider Brand B to be a separate unit of accounting for purposes of testing impairment because that brand is managed separately from Brand A and is used exclusively by a separate asset group under the Impairment or Disposal of Long-Lived Assets Subsections of Subtopic 360-10.

The unit of account used for purposes of testing an indefinite-lived intangible asset for impairment might change over time; therefore, at each impairment testing date, an entity should reassess whether that asset should be tested as an individual asset or instead be combined with one or more other indefinite-lived intangible assets as a single unit of account. If there is a change in the asset's unit of account during the period, ASC 350-30-35-27 requires an entity to first test the asset for impairment as an individual asset before testing it as part of a combined unit of account.

ASC 350-30-35-26

All of the following shall be included in the determination of the unit of accounting used to test indefinite-lived intangible assets for impairment:

a. The unit of accounting shall include only indefinite-lived intangible assets—those assets cannot be tested in combination with goodwill or with a finite-lived asset.

b. The unit of accounting cannot represent a group of indefinite-lived intangible assets that collectively constitute a business or a nonprofit activity.

c. A unit of accounting may include indefinite-lived intangible assets recorded in the separate financial statements of consolidated subsidiaries. As a result, an impairment loss recognized in the consolidated financial statements may differ from the sum of the impairment losses (if any) recognized in the separate financial statements of those subsidiaries.

ASC 350-30-35-27

If, based on a change in the way in which intangible assets are used, an entity combines as a unit of accounting for impairment testing purposes indefinite-lived intangible assets that were previously tested for impairment separately, those intangible assets shall be separately tested for impairment in accordance with paragraphs 350-30-35-18 through 35-20 prior to being combined as a unit of accounting.

2.3 When to perform a quantitative impairment test

According to ASC 350-30-35-18, indefinite-lived intangible assets (and indefinite-lived intangible assets that are combined as one unit of account) should be tested for impairment at the individual asset (or unit of account) level on an annual basis or more frequently if a triggering event occurs between annual tests indicating that it is more likely than not that the fair value of the indefinite-lived intangible asset (or unit of account) is less than its carrying amount (in other words, the asset is impaired).

ASC 350-30-35-18

An intangible asset that is not subject to amortization shall be tested for impairment annually and more frequently if events or changes in circumstances indicate that it is more likely than not that the asset is impaired.

2.3.1 Annual impairment test date considerations

An entity is allowed to establish any date during the fiscal year as the annual impairment test date, as long as the test is performed consistently on the same date each year.

Grant Thornton insight: Annual impairment testing date for indefinite-lived intangible assets

ASC 350-30 does not discuss the timing of the annual impairment testing date for indefinite-lived intangible assets. However, in practice, the annual impairment testing date is established similar to how the annual goodwill impairment test is established (as discussed in Section 3.2.1, "Establishing the annual goodwill impairment test date"). In other words, an entity can establish any date during the fiscal year as the annual test date as long as the test is performed on the same date each year.

Annual testing dates selected closer to the financial reporting date reduce the chance of a triggering event occurring after the annual impairment testing date, but before the financial reporting date. However, entities should take into consideration the time necessary to complete the annual impairment test, ensuring that they select a date early enough to provide sufficient time to complete the test before the release of the financial statements.

A change in the annual testing date is considered to be a change in accounting principle that must comply with the requirements under ASC 250.

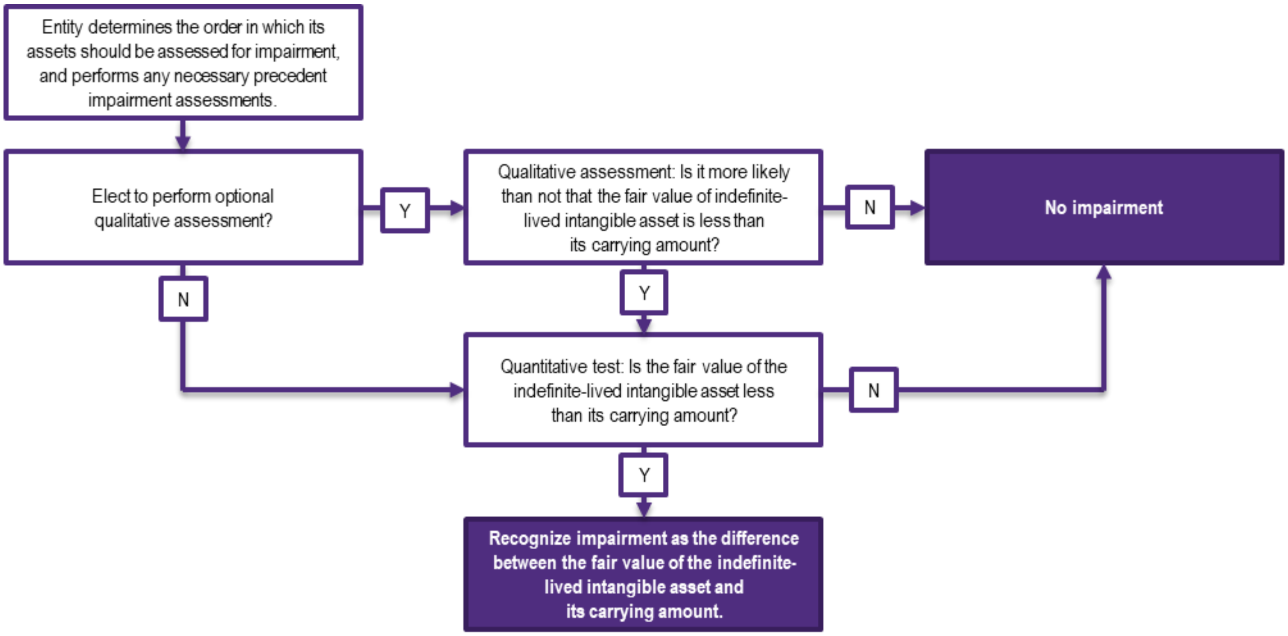
2.3.2 Qualitative impairment testing considerations

When performing an annual impairment test, an entity has the option to first use qualitative factors to determine whether it is more likely than not that an indefinite-lived intangible asset is impaired. This qualitative test may be used as a basis for determining whether it is necessary to perform a quantitative impairment test. If, as a result of the qualitative test, an entity determines that it is more likely than not that an impairment exists, the entity is required to perform a quantitative impairment test.

Conversely, if an entity passes the qualitative test and determines that an impairment more likely than not does not exist, the entity is not required to perform a quantitative impairment test. Since the qualitative test is optional, an entity may decide to bypass the qualitative assessment for its annual impairment test and perform the quantitative test, as discussed in Section 2.4, "Quantitative impairment test."

Figure 4 provides an overview of the annual impairment testing model when determining whether to perform a qualitative impairment test.

Figure 4: Annual impairment testing model for indefinite-lived intangible assets



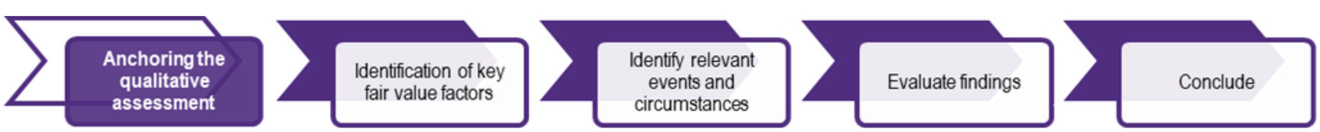
The guidance in ASC 350 provides factors to consider when using the qualitative impairment assessment to determine whether it is more likely than not that an indefinite-lived intangible is impaired and a quantitative impairment test should be performed.

The main objective of the qualitative impairment assessment is twofold:

- To document the reporting entity's assessment of events and circumstances that would be used as inputs in estimating the fair value of the intangible asset; and
- To determine whether those events and circumstances indicate, as of the date of the qualitative assessment, that the asset's fair value is more likely than not less than its carrying amount.

Often, this qualitative analysis is an assessment of how events and circumstances have changed since the reporting entity last formally estimated the fair value of the intangible asset. (See "Qualitative factors to consider" below, which includes a list of qualitative events and circumstances that entities should consider.) These factors, which relate to how events and circumstances have changed, are evaluated both individually and together with other factors to determine whether it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying amount.

To better understand the qualitative assessment process for indefinite-lived intangibles, we believe the following diagram illustrates certain "steps" that may prove helpful when performing a qualitative assessment.



Step 1: Anchoring the qualitative assessment

The first step in the qualitative assessment process is to "anchor" the assessment to the margin between the most recent estimate of the intangible asset's fair value and the asset's carrying value. Generally, the larger the margin between the most recent fair value and the asset's carrying value, and the more recent the fair value calculation is, the more likely it will be that an entity may rely on the most recent fair value as a basis for the qualitative assessment. Conversely, the more time that has elapsed since the fair value calculation, the more challenging it is to use that fair value for the qualitative assessment. In addition, if fair value significantly exceeds the asset's carrying value, these larger amounts of excess fair value may be able to absorb a larger quantity of, as well as more significant, negative changes in events and circumstances that could potentially impact the asset's fair value. If the margin between the asset's last fair value determination and the current carrying value is narrow, it would require more positive events and circumstances to overcome a more-likely-than-not assessment that an asset is impaired. See Section 3.2.2, "Optional qualitative goodwill assessment," for further discussion.

Step 2: Identify the main factors affecting the fair value calculation:

The second step of the qualitative impairment test assessment is to identify the main factors affecting the fair value calculation. An entity should understand the key assumptions and significant inputs that drive the fair value calculation of each asset being evaluated in the qualitative analysis. Since the quantitative impairment test compares the fair value of the indefinite-lived intangible asset to its carrying value, a significant component of a qualitative assessment is identifying the key inputs used in estimating the asset's fair value.

Step 3: Identify events and circumstances

Once the entity has identified the key assumptions and inputs to the fair value calculation of each asset, it should determine whether any events or circumstances have occurred since the last impairment testing date that could affect an asset's fair value. Some examples of events and circumstances are outlined in ASC 350-30-35-18B (and are listed below in "Qualitative factors to consider"). Understanding those factors that primarily affect the asset's fair value will help an entity identify any changes in events and circumstances that pertain to those identified factors. All relevant changes in facts and circumstances since the last time when fair value was formally calculated should be identified.

Step 4: Evaluate findings

The fourth step of the qualitative impairment test assessment is to evaluate the findings from the previous steps of the assessment. An entity must weigh all factors in their totality in order to form a conclusion about whether it is more likely than not that the asset is impaired. While identifying factors and events may be straightforward, the weighting of various factors requires a great deal of professional judgment. In general, greater weight is given to those factors that most affect an asset's fair value. An entity may also consider using a sensitivity analysis to help quantify which factors most affect fair value.

Step 5: Conclude on results

The final step of the qualitative impairment test assessment is to determine whether the qualitative assessment results indicate that an asset is more likely than not impaired. If the entity concludes that the asset is more likely than not impaired, the next step is to apply the quantitative test to calculate impairment loss.

Qualitative factors to consider

The guidance in ASC 350-30-35-18B outlines some of the qualitative factors to be considered in assessing whether it is more likely than not that an indefinite-lived intangible asset is impaired. As indicated in ASC 350-30-35-18C, the factors listed are not all-inclusive; therefore, an entity should consider other relevant events and circumstances that might affect the significant inputs used to determine the fair value of the indefinite-lived intangible asset.

ASC 350-30-35-18B

In assessing whether it is more likely than not that an indefinite-lived intangible asset is impaired, an entity shall assess all relevant events and circumstances that could affect the significant inputs used to determine the fair value of the indefinite-lived intangible asset. Examples of such events and circumstances include the following:

a. Cost factors such as increases in raw materials, labor, or other costs that have a negative effect on future expected earnings and cash flows that could affect significant inputs used to determine the fair value of the indefinite-lived intangible asset

b. 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 that could affect significant inputs used to determine the fair value of the indefinite-lived intangible asset

c. Legal, regulatory, contractual, political, business, or other factors, including asset-specific factors that could affect significant inputs used to determine the fair value of the indefinite-lived intangible asset

d. Other relevant entity-specific events such as changes in management, key personnel, strategy, or customers; contemplation of bankruptcy; or litigation that could affect significant inputs used to determine the fair value of the indefinite-lived intangible asset

e. 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 (in both absolute terms and relative to peers), or a change in the market for an entity's products or services due to the effects of obsolescence, demand, competition, or other economic factors (such as the stability of the industry, known technological advances, legislative action that results in an uncertain or changing business environment, and expected changes in distribution channels) that could affect significant inputs used to determine the fair value of the indefinite-lived intangible asset

f. Macroeconomic conditions such as deterioration in general economic conditions, limitations on accessing capital, fluctuations in foreign exchange rates, or other developments in equity and credit markets that could affect significant inputs used to determine the fair value of the indefinite-lived intangible asset.

ASC 350-30-35-18C

The examples included in the preceding paragraph are not all-inclusive, and an entity shall consider other relevant events and circumstances that could affect the significant inputs used to determine the fair value of the indefinite-lived intangible asset. An entity shall consider the extent to which each of the adverse events and circumstances identified could affect the significant inputs used to determine the fair value of an indefinite-lived intangible asset. An entity also shall consider the following to determine whether it is more likely than not that the indefinite-lived intangible asset is impaired:

a. Positive and mitigating events and circumstances that could affect the significant inputs used to determine the fair value of the indefinite-lived intangible asset

b. If an entity has made a recent fair value calculation for an indefinite-lived intangible asset, the difference between that fair value and the then carrying amount

c. Whether there have been any changes to the carrying amount of the indefinite-lived intangible asset.

The existence of a single event or circumstance from the examples listed in ASC 350-30-35-18B and 35-18C may not, on its own, require an entity to perform a quantitative test. Likewise, the existence of a single positive or mitigating event or circumstance does not represent a rebuttable presumption that a quantitative impairment test is unnecessary. Once an entity identifies the factors relevant to its qualitative assessment, it should weigh each factor according to its effect on the qualitative analysis, as well as assess the totality of the events and circumstances identified based on the guidance in ASC 350-35-18B and 35-18C, to determine whether the asset's fair value is more likely than not less than its carrying amount. If an entity determines, based on the qualitative assessment, that it is not more likely than not that an indefinite-lived intangible asset is impaired, then no quantitative test is required. If an entity determines from a qualitative assessment that it is more likely than not that an indefinite-lived intangible asset is impaired, then a quantitative test should be performed, as discussed in Section 2.4, "Quantitative impairment test."

See Section 3.2.2, "Optional qualitative goodwill assessment," for further discussion on this topic.

2.3.3 Impairment testing indicators between annual tests

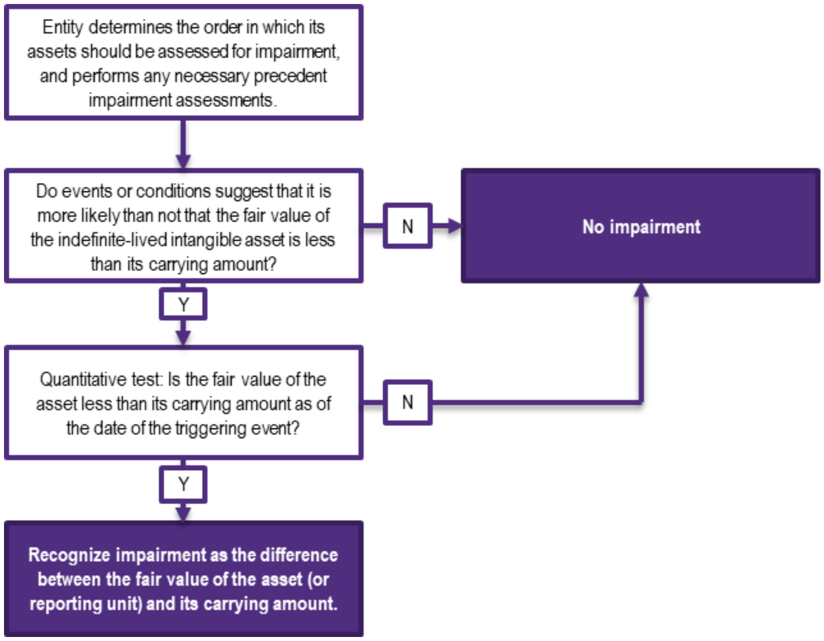
An entity is required to test its indefinite-lived intangible assets for impairment on a date other than its annual impairment testing date if events or changes in circumstances indicate that it is more likely than not that the asset is impaired.

An entity must refer to factors (a) through (f) described in ASC 350-30-35-18B and the other impairment indicators in ASC 350-30-35-18C not only for purposes of performing a qualitative assessment as part of its annual evaluation, but also for determining whether an indefinite-lived intangible asset should be tested for impairment between annual testing dates. Some common examples of events or changes in circumstances that might require an interim impairment test include a decrease in the asset's market price, an adverse change in the asset's use, an adverse change in legal or business climate losses in the current period or expected losses in future periods, or changes to inputs used to value an indefinite-lived intangible asset.

If an event or change in circumstance that occurs between annual testing dates indicates that an asset might be impaired, an entity is required to assess the indefinite-lived intangible asset(s) for impairment by performing the quantitative test. The date on which the impairment test is performed is the date when the event or circumstance occurs that indicates the asset is more likely than not impaired.

Figure 5 provides an overview of the interim impairment testing model for indefinite-lived intangible assets between annual impairment tests.

Figure 5: Interim impairment testing model for indefinite-lived intangible assets



Grant Thornton insight: Events and circumstances indicating an interim impairment test should be performed

For entities that report their financial results annually and perform annual impairment analyses at or near their fiscal year-end, an impairment analysis is also performed on the date when it is determined that an event or an accumulation of events or changes in circumstances exist that indicate the carrying amount of the indefinite-lived intangible asset may not be recovered. In these instances, the impairment analysis may not be deferred to the entity's fiscal year-end or to the annual impairment testing date if such testing date is other than at year-end. Subsequent unforeseen recovery or improvements in conditions (such as an unforeseen transaction or an unforeseen spike in market-based pricing) do not eliminate the requirement to perform an impairment analysis in response to an event or circumstances that require impairment testing, even if the recovery occurs between the impairment testing date and the entity's fiscal year end.

Further, entities performing impairment analyses as a result of an event or changes in circumstances that indicate potential impairment should only consider information that is known or knowable at the time of those events. While entities may take advantage of hindsight to a limited degree in completing these analyses, factors or data used in such circumstances are limited to those that would have been reasonably projected at the impairment testing date.

2.4 Quantitative impairment test

An entity is required to perform a quantitative impairment test if it determines that it is more likely than not that an indefinite-lived intangible asset is impaired, regardless of whether it is an annual impairment evaluation or an assessment of a triggering event at an interim date. In performing a quantitative test, the entity should determine, and then compare, the fair value of the individual indefinite-lived intangible asset to its carrying amount. If the fair value is less than the carrying amount, the difference is the impairment loss, which an entity recognizes in earnings. Once an impairment loss is recognized, the carrying value of the indefinite-lived intangible asset is also adjusted for the amount of the impairment charge to arrive at its new cost basis; subsequent reversal of any impairment charge is not allowed. If the fair value of the individual asset exceeds the carrying amount of the indefinite-lived intangible asset, then no impairment should be recognized.

ASC 350-30-35-19

The quantitative impairment test for an indefinite-lived intangible asset shall consist of a comparison of the fair value of the asset with its carrying amount. If the carrying amount of an intangible asset exceeds its fair value, an entity shall recognize an impairment loss in an amount equal to that excess. After an impairment loss is recognized, the adjusted carrying amount of the intangible asset shall be its new accounting basis.

3. Goodwill

The guidance in ASC 350-20 requires entities to test goodwill for impairment not only on an annual basis, but in between annual testing dates if circumstances or conditions indicate that it is more likely than not that the fair value of a reporting unit is below its carrying amount. Goodwill is impaired when the carrying amount of the reporting unit, including goodwill, exceeds its fair value.

An entity may elect to first assess qualitative factors to determine whether it is necessary to perform a quantitative annual goodwill impairment test. An entity making this election is not required to calculate the fair value of a reporting unit unless it concludes that it is more likely than not that the reporting unit's fair value is less than its carrying amount.

Goodwill is tested for impairment only after other assets requiring impairment testing in a reporting unit are tested for impairment. This testing order is necessary because goodwill cannot be directly measured, but is rather a residual asset at the reporting unit level. In practice, identifying the potential impairment of goodwill means that an entity should first consider whether other assets are impaired. A goodwill triggering event for an impairment test could indicate that there is impairment of the entity's other assets. For more on the order of impairment testing, please see Section 1.

Under ASC 350-20, goodwill is impaired when the carrying amount of the reporting unit, including goodwill, exceeds its fair value. Goodwill impairment is limited, however, to the total amount of goodwill allocated to that reporting unit. ASC 350-20-35-1 through 35-3 provides an overview of the accounting and impairment testing for goodwill after it has been initially recognized in a business combination transaction.

ASC 350-20-35-1

Goodwill shall not be amortized. Instead, goodwill shall be tested for impairment at a level of reporting referred to as a reporting unit. (Paragraphs 350-20-35-33 through 35-46 provide guidance on determining reporting units.)

ASC 350-20-35-2

Impairment is the condition that exists when the carrying amount of goodwill exceeds its fair value. A goodwill impairment loss is recognized for the amount that the carrying amount of a reporting unit, including goodwill, exceeds its fair value, limited to the total amount of goodwill allocated to that reporting unit. However, an entity shall consider the related income tax effect from any tax deductible goodwill, if applicable, in accordance with paragraph 350-20-35-8B when measuring the goodwill impairment loss.

ASC 350-20-35-3

An entity may first assess qualitative factors, as described in paragraphs 350-20-35-3A through 35-3G, to determine whether it is necessary to perform the quantitative goodwill impairment test discussed in paragraphs 350-20-35-4 through 35-13. If determined to be necessary, the quantitative impairment test shall be used to identify goodwill impairment and measure the amount of a goodwill impairment loss to be recognized (if any).

At the crossroads: ASU 2017-04 on simplifying the goodwill impairment test

In January 2017, the FASB issued ASU 2017-04 to reduce the cost and complexity of subsequent accounting for goodwill. The ASU amends how an entity measures a goodwill impairment loss by eliminating the second step of the annual or interim goodwill impairment test. That second step requires entities to calculate the implied fair value of goodwill by determining the fair value of the net identifiable assets and liabilities of the reporting unit, similar to accounting for a business combination. However, under the amended guidance, entities are only required to perform a single-step quantitative test to identify and measure goodwill impairment, which compares the fair value of the reporting unit to its carrying amount.

The amendments in the ASU are effective for annual and interim impairment testing in periods beginning after December 15, 2019 for public business entities and in periods beginning after December 15, 2021 for all other entities. Early adoption is permitted for both interim and annual impairment tests performed with a measurement date after January 1, 2017.

This Viewpoint includes the accounting guidance for entities that have adopted the amendments in ASU 2017-04. Entities that have not yet adopted these amendments should refer to ASC 350-20 for guidance related to Step 2 of the goodwill impairment test. See Section 4 in this document for guidance that applies to private companies that have adopted the private company accounting alternatives.

3.1 Reporting units

A reporting unit is the unit of account at which goodwill is tested for impairment. Accordingly, before performing a goodwill impairment assessment, an entity should first identify its reporting unit(s) and assign goodwill to those reporting units. ASC 280 defines a "reporting unit" as follows.

Reporting Unit

The 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).

The determination of reporting units begins with applying the guidance in ASC 280 to identify an entity's operating segments. (See Grant Thornton's *Segment reporting: More than just disclosure* for help in navigating the complexities involved in identifying operating segments under ASC 280, which is key to the appropriate determination of reporting units for both public and nonpublic entities.)

3.1.1 Identifying the reporting unit

When determining the reporting units for goodwill impairment testing, an entity must consider whether a reporting unit resides at the operating segment level or at the component level, which is one level below the operating segment. A component of an operating segment is considered to be a reporting unit if both

- The component is a business (or nonprofit activity) that makes available discrete financial information; and
- “Segment management,” as defined in ASC 280-10-50-7, regularly reviews the component’s operating results.

ASC 280-10-50-7

Generally, an operating segment has a segment manager who is directly accountable to and maintains regular contact with the chief operating decision maker to discuss operating activities, financial results, forecasts, or plans for the segment. The term *segment manager* identifies a function, not necessarily a manager with a specific title.

Improper identification of a reporting unit could lead to an inappropriate conclusion about goodwill impairment. The operating segment is the highest level at which an entity may identify a reporting unit. Therefore, an entity has at least as many reporting units as operating segments, though it may have more.

ASC 350-30-35-33 through 35-38 provides guidance for determining a reporting unit.

ASC 350-20-35-33

The provisions of Topic 280 shall be used to determine the reporting units of an entity.

ASC 350-20-35-34

A component of an operating segment is a reporting unit if the component constitutes a business or a nonprofit activity for which discrete financial information is available and segment management, as that term is defined in paragraph 280-10-50-7, regularly reviews the operating results of that component. Subtopic 805-10 includes guidance on determining whether an asset group constitutes a business. Throughout the remainder of this Section, the term business also includes a nonprofit activity.

ASC 350-20-35-36

An operating segment shall be deemed to be a reporting unit if all of its components are similar, if none of its components is a reporting unit, or if it comprises only a single component.

ASC 350-20-35-37

Reporting units will vary depending on the level at which performance of the segment is reviewed, how many businesses the operating segment includes, and the similarity of those businesses. In other words, a reporting unit could be the same as an operating segment, which could be the same as a reportable segment, which could be the same as the entity as a whole (entity level).

ASC 350-20-35-38

An entity that is not required to report segment information in accordance with Topic 280 is nonetheless required to test goodwill for impairment at the reporting unit level. That entity shall use the guidance in paragraphs 280-10-50-1 through 50-9 to determine its operating segments for purposes of determining its reporting units.

ASC 350-20-55-1 through 55-9 shows how to apply the guidance on determining a reporting unit, as described in ASC 350-20-35-33 through 35-38. As noted in ASC 350-20-35-34, there are three characteristics that must be present for a component of an operating segment to be a reporting unit: The component must constitute a business (or a nonprofit activity), there must be discrete financial information that is available, and that information must be regularly reviewed by segment management. The determination of what constitutes a reporting unit requires judgment and is based on an analysis of the facts and circumstances in each situation.

When assessing the criteria for determining whether a component qualifies as a reporting unit, entities should consider the following:

- *Constitutes a business (or nonprofit activity)* – The first requirement for a component to qualify as a reporting unit is that it must constitute a “business” (or a nonprofit activity), as defined in ASC 805-10-55-3A through 55-6 and in ASC 805-10-55-8 through 55-9.

  While this typically means that the component generates revenue and incurs expenses, these activities are not a requirement for the component to qualify as a business. Likewise, the fact that revenue and expenses exist and that operating information is prepared for a component does not always mean that the component constitutes a business. For instance, the revenue and expenses may relate to a particular brand or product line integral to another business operation, but the component is not being operated as a business on its own.

  In addition, a component that sells exclusively to other components within the same entity may be considered a business. A component that is engaged in business activities that do not generate revenue could also qualify as a business. For example, a start-up operation that has not yet earned revenue may qualify as a business. Similarly, a research and development component could be engaged in business activities and might therefore qualify as a business, even though it does not yet generate revenue.

  For a component of a nonprofit entity to qualify as a reporting unit, it must be a nonprofit activity. The definition of a nonprofit activity in the Master Glossary from the FASB Codification is as follows.

Nonprofit Activity

An integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing benefits, other than goods or services at a profit or profit equivalent, as a fulfillment of an entity’s purpose or mission (for example, goods or services to beneficiaries, customers, or members). As with a not-for-profit entity, a nonprofit activity possesses characteristics that distinguish it from a business or a for-profit business entity.

For purposes of the remainder of this publication, a business or a nonprofit activity is referred to as a "business."

- *Discrete financial information is available* – Another characteristic that must exist for a component to qualify as a reporting unit is that discrete financial information for the component is available. According to the guidance in ASC 280, "discrete financial information" does not need to comprise a full set of GAAP financial statements. The primary consideration in determining whether discrete financial information is available for a product line, geographic area, or other operating component is whether the information is provided in sufficient detail to allow the segment manager to assess performance and make resource allocations. A complete balance sheet as part of the financial information provided to the segment manager is not necessary to have a reporting unit. If there is only income statement information provided to the segment manager, the entity will need to allocate assets and liabilities to the reporting unit. See "Allocating assets and liabilities to reporting units" on page 56 for guidance on assigning assets and liabilities to reporting units when only income statement information is available and the component meets the other requirements to be a reporting unit.
- *Operating results are regularly reviewed by segment management* – When determining whether a component qualifies as a reporting unit, the focus is on how the components are managed by segment managers and what information those segment managers use to make operating decisions and to assess performance. The approach used to review operating results when determining reporting units is similar to how the management approach is used to identify an operating segment in ASC 280—that is, look at how management has organized the entity to make key operating decisions and to assess performance.

ASC 350-20-55-3 to 55-5 also provides implementation guidance that should be considered when determining reporting units.

ASC 350-20-55-3

The determination of whether a component constitutes a business or a nonprofit activity requires judgment based on specific facts and circumstances. The guidance in Section 805-10-55 should be considered in determining whether a group of assets constitutes a business or a nonprofit activity.

ASC 350-20-55-4

The term discrete financial information should be applied in the same manner that it is applied in determining operating segments in accordance with paragraph 280-10-50-1. That guidance indicates that it is not necessary that assets be allocated for a component to be considered an operating segment (that is, no balance sheet is required). Thus, discrete financial information can constitute as little as operating information. Therefore, in order to test goodwill for impairment in accordance with this Subtopic, an entity may be required to assign assets and liabilities to reporting units (consistent with the guidance in paragraphs 350-20-35-39 through 35-40).

ASC 350-20-55-5

Segment management, as defined in paragraphs 280-10-50-7 through 50-8, is either a level below or the same level as the chief operating decision maker. According to Topic 280, a segment manager is directly accountable to and maintains regular contact with the chief operating decision maker to discuss operating activities, financial results, forecasts, or plans for the segment. The approach used in this Subtopic to determine reporting units is similar to the one used to determine operating segments; however, this Subtopic focuses on how operating segments are managed rather than how the entity as a whole is managed; that is, reporting units should reflect the way an entity manages its operations.

3.1.2 Aggregating components into a single reporting unit

Entities may aggregate components of an operating segment into a single reporting unit if the components share similar economic characteristics. However, components of different operating segments should not be aggregated, even if they have similar economic characteristics. The guidance in ASC 280-10-50-11 and 50-13 outlines the aggregation criteria to be used when determining whether components of an operating segment may be aggregated for purposes of determining reporting units.

ASC 350-20-35-35

However, two or more components of an operating segment shall be aggregated and deemed a single reporting unit if the components have similar economic characteristics. Paragraph 280-10-50-11 shall be considered in determining if the components of an operating segment have similar economic characteristics.

When determining whether reporting units have similar economic characteristics, entities should consider all of the factors outlined in ASC 280-10-50-11. Economically similar components would also be expected to have similar long-term average gross margins. Consistent with ASC 280-10-50-11, entities may aggregate components that have similar economic characteristics, as well as other similar characteristics, as follows:

- Products and services
- Production processes
- Type or class of customer for their products and services
- Methods to distribute products or provide services
- Regulatory environment if applicable (for example, banking, insurance, public utilities)

Unlike the guidance in ASC 280 that requires all of the factors listed above to be similar in order to aggregate operating segments, the FASB indicated in EITF Issue D-101 that the Board did not intend that entities should meet *every* factor listed in ASC 280-10-50-11 for two components to be considered economically similar and therefore eligible for aggregation as a single reporting unit. Other factors that should be considered in addition to those factors in ASC 280-10-50-11 are indicated in ASC 350-20-55-7 and include, but are not limited to, the following:

- The manner in which an entity operates its business or nonprofit activity and the nature of those operations
- Whether goodwill is recoverable from the separate operations of each component business (or nonprofit activity) or from two or more component businesses (or nonprofit activities) working in concert, which might be the case if the components are economically interdependent
- The extent to which the component businesses (or nonprofit activities) share assets and other resources, which might be evidenced by extensive transfer pricing mechanisms
- Whether the components support and benefit from common research and development projects

Components of different operating segments cannot be aggregated into a single reporting unit.

As indicated in the implementation guidance in ASC 350-20-55-6 through 55-9, the determination of a reporting unit begins at the operating segment level, meaning that each operating segment is considered to be a reporting unit, at a minimum, unless the operating segment has additional components that would be considered reporting units. The reporting unit determination begins with how the segment manager reviews segment information for resource allocations to components that represent businesses with discrete financial information within an operating segment.

ASC 350-20-55-6

Evaluating whether two components have similar economic characteristics is a matter of judgment that depends on specific facts and circumstances. That assessment should be more qualitative than quantitative.

ASC 350-20-55-7

In determining whether the components of an operating segment have similar economic characteristics, all of the factors in paragraph 280-10-50-11 should be considered. However, every factor need not be met in order for two components to be considered economically similar. In addition, the determination of whether two components are economically similar need not be limited to consideration of the factors described in that paragraph. In determining whether components should be combined into one reporting unit based on their economic similarities, factors that should be considered in addition to those in that paragraph include, but are not limited to, the following:

a. The manner in which an entity operates its business or nonprofit activity and the nature of those operations

b. Whether goodwill is recoverable from the separate operations of each component business (or nonprofit activity) or from two or more component businesses (or nonprofit activities) working in concert (which might be the case if the components are economically interdependent)

c. The extent to which the component businesses (or nonprofit activities) share assets and other resources, as might be evidenced by extensive transfer pricing mechanisms

d. Whether the components support and benefit from common research and development projects.

The fact that a component extensively shares assets and other resources with other components of the operating segment may be an indication that the component either is not a business or nonprofit activity or it may be economically similar to those other components.

ASC 350-20-55-8

Components that share similar economic characteristics but relate to different operating segments may not be combined into a single reporting unit. For example, an entity might have organized its operating segments on a geographic basis. If its three operating segments (Americas, Europe, and Asia) each have two components (A and B) that are dissimilar to each other but similar to the corresponding components in the other operating segments, the entity would not be permitted to combine component A from each of the operating segments to make reporting unit A.

ASC 350-20-55-9

If two operating segments have been aggregated into a reportable segment by applying the aggregation criteria in paragraph 280-10-50-11, it would be possible for one or more of those components to be economically dissimilar from the other components and thus be a reporting unit for purposes of testing goodwill for impairment. That situation might occur if an entity's operating segments are based on geographic areas. The following points need to be considered in addressing this circumstance:

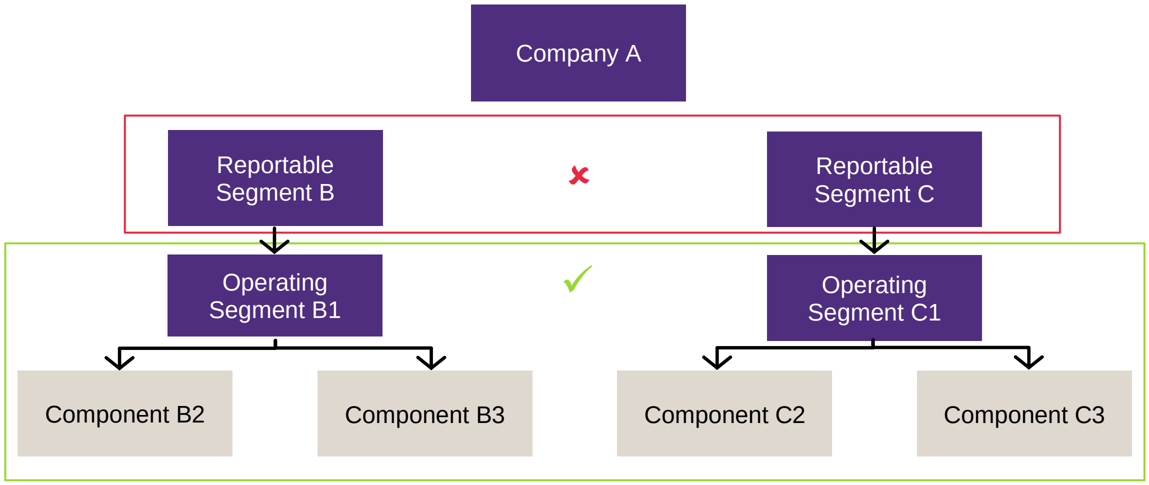
a. The determination of reporting units under this Subtopic begins with the definition of an operating segment in paragraph 280-10-50-1 and considers disaggregating that operating segment into economically dissimilar components for the purpose of testing goodwill for impairment. The determination of reportable segments under Topic 280 also begins with an operating segment, but considers whether certain economically similar operating segments should be aggregated into a single operating segment or into a reportable segment

b. The level at which operating performance is reviewed differs between this Subtopic and Topic 280. It is the chief operating decision maker who reviews operating segments and the segment manager who reviews reporting units (components of operating segments). Therefore, a component of an operating segment would not be considered an operating segment for purposes of that Topic unless the chief operating decision maker regularly reviews its operating performance; however, that same component might be a reporting unit under this Subtopic if a segment manager regularly reviews its operating performance (and if other reporting unit criteria are met).

Illustrative example of reporting units

Company A has two reportable segments, B and C. Reportable segments can be an aggregation of two or more operating segments that meet the aggregation criteria in ASC 280 or can be individual operating segments that meet the quantitative thresholds in ASC 280 to be disclosed separately in the financial statements. Company A also has two operating segments, B1 and C1. Each of the company's operating segments has two components, as shown in the diagram below.

In this example, Company A has a minimum of two reporting units, Operating Segments B1 and C1, because an entity must have at least as many reporting units as operating segments. In addition, Company A may have up to four reporting units, because each component below the two operating segments might also qualify as a reporting unit if they meet the criteria to be a business with discrete financial information reviewed by a segment manager, and the components do not meet the aggregation criteria described in ASC 350-20-55-7. Company A is allowed to aggregate only components that are within the same operating segment. For example, Component B3 cannot be combined with Component C3 because they belong to different operating segments.



Grant Thornton insight: Monitoring for changes in operating segments and reporting units

Over time, an entity's conclusion regarding its operating segments may change, reflecting changes in the entity's management structure resulting from acquisitions, restructurings, dispositions, and reorganizations, or simply due to changes in the financial information used by the chief operating decision maker or segment management to monitor the entity's performance. A change in operating segments will result in a change in reporting units. An entity needs to continually monitor its segment and reporting unit determinations to make sure that a change in the entity's reporting unit structure has not occurred. A goodwill impairment test is generally required when an entity changes its reporting units. See Section 3.2.3, "Other circumstances requiring impairment testing," for the impairment testing guidance when an entity's reporting units have changed.

3.2 When to perform a quantitative impairment test for goodwill

Goodwill must be tested for impairment at the reporting unit level at least annually on the same annual testing date. When performing this annual test, an entity has the option to first assess qualitative factors to determine whether a quantitative goodwill impairment test is required. The qualitative assessment is discussed in greater detail in Section 3.2.2, "Optional qualitative goodwill assessment."

Goodwill must also be tested for impairment between annual test dates if events or circumstances indicate that it is more likely than not that the fair value of a reporting unit is below its carrying amount. Additionally, when an entity changes the composition of its reporting units, including changes due to disposals or reorganizations, the entity may need to test goodwill for impairment both before and after those changes. See Section 3.2.3, "Other circumstances requiring impairment testing," for additional information.

3.2.1 Establishing the annual goodwill impairment test date

An entity may establish any date during the fiscal year as the annual testing date for goodwill impairment as long as the test is performed on the same date each year, based on the guidance in ASC 350-20-35-28. An entity may have different annual test dates for different reporting units; however, the annual testing date for each reporting unit must be consistent from year to year.

ASC 350-20-35-28

Goodwill of a reporting unit shall be tested for impairment on an annual basis and between annual tests in certain circumstances (see paragraph 350-20-35-30). 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.

Grant Thornton insight: Choosing an annual impairment testing date

Selecting an annual test date closer to the financial reporting date reduces the chance of a triggering event occurring after the annual goodwill testing date but before the financial reporting date. However, entities should take into consideration the time necessary to complete the annual impairment test, ensuring that they select a date early enough to provide sufficient time to complete the test before the release of the financial statements.

An entity with a large number of reporting units may decide to spread the testing efforts throughout the year based on the availability of testing resources. When an entity selects different annual test dates for different reporting units, they should consider the amount of time and effort needed to determine the fair value of reporting units that are *not* being tested for impairment at that same time in order to reconcile the fair value of the individual reporting units to the public entity's market capitalization to ensure that the individual reporting units being tested have been appropriately valued (see discussion of the market capitalization reconciliation considerations in Section 3.3.4, "Control premiums").

Changing the annual testing date

In certain situations, an entity may elect to change the date of the annual goodwill impairment test, for example, if an entity makes a significant acquisition and decides to align its annual testing date with that of the acquired entity. A change in the annual impairment testing date would constitute a change in accounting principle under ASC 250 and should only be made if the change in date is determined to be preferable.

ASC 250-10-45-2

A reporting entity shall change an accounting principle only if either of the following apply:

a. The change is required by a newly issued Codification update.

b. The entity can justify the use of an allowable alternative accounting principle on the basis that it is preferable.

Grant Thornton insight: SEC views on accounting principle change related to a change in annual impairment test date

In the past, the SEC staff required a public entity that changed its annual goodwill impairment testing date to file a preferability letter, regardless of the materiality of the effect of the change. At the 2014 AICPA Conference on Current SEC and PCAOB Developments, the SEC staff announced that it would no longer request that registrants file a preferability letter for a change in annual impairment test date as long as both of the following criteria are met:

- The change does not represent a material change to the registrant's method of applying an accounting principle.
- The change is prominently disclosed in the registrant's financial statements.

Further, the SEC staff has also commented that not more than 12 months should elapse between impairment tests and that entities should not initiate a change in the annual impairment testing date in an effort to manipulate earnings by accelerating or deferring impairment charges. As a result, an entity that changes its annual testing date may be required to perform more than one annual impairment test in the year of change. In addition, the SEC staff will likely raise concerns if a registrant frequently changes the date of its annual goodwill impairment test.

Changing the annual impairment testing date

A calendar-year public entity has a June 1 annual goodwill impairment testing date for its reporting units. The entity acquires a new significant business operation on October 1, 20X1, which comprises a separate reporting unit. Because of the significance of the acquisition, the entity simultaneously decides to change its annual goodwill impairment testing date to October 1 for all of its reporting units and determines that the change in testing date is preferable. Since October 1 is chosen as the annual impairment testing date, the entity must perform an annual goodwill impairment test for the existing reporting units on October 1, 20X1 in addition to the annual goodwill impairment test previously performed only four months earlier on June 1, 20X1. If the entity waited until October 1, 20X2 to perform the annual goodwill impairment test, more than 12 months would have elapsed since the June 1, 20X1 annual goodwill impairment test of the entity's original reporting units. As a result, in this situation, the entity would perform two annual impairment tests within one year.

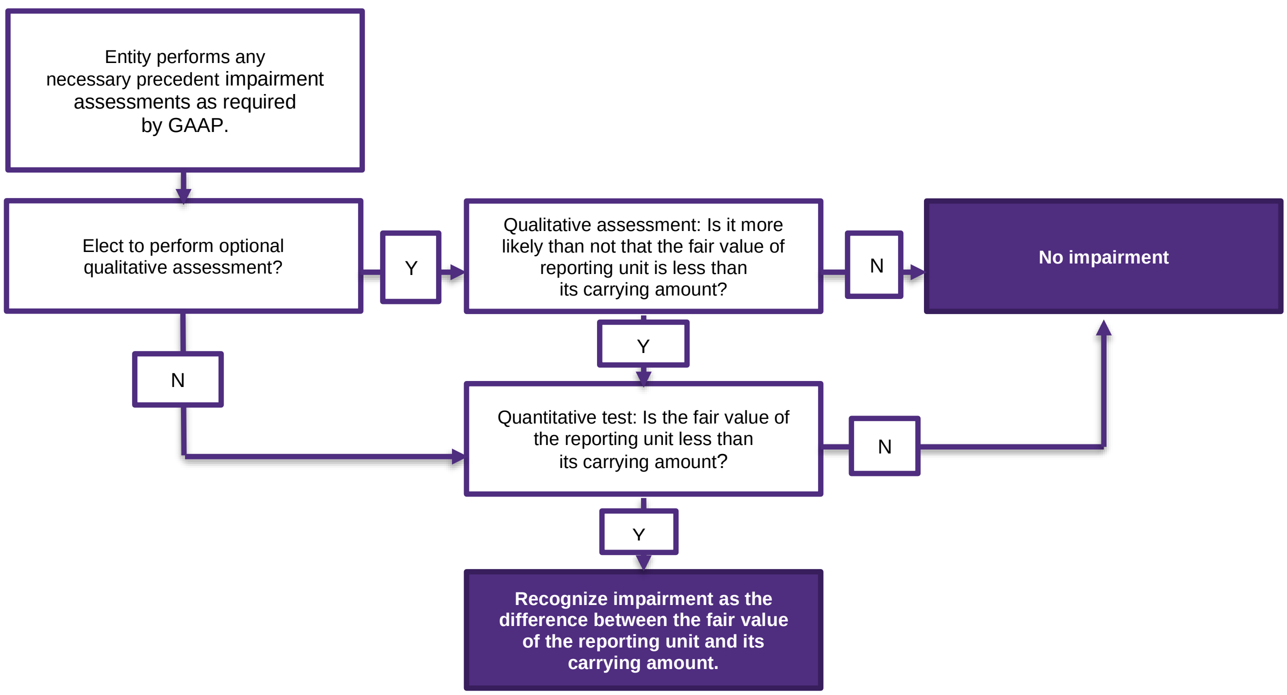
3.2.2 Optional qualitative goodwill assessment

When performing an annual impairment test, entities have the option to first qualitatively assess whether it is more likely than not that a reporting unit's fair value is less than its carrying amount. This qualitative test is used as a basis for determining whether it is necessary to perform a quantitative impairment test. If the reporting unit passes the qualitative test because management determines that it is not more likely than not that the reporting unit's fair value is less than its carrying amount, the entity is not required to perform a quantitative test. On the other hand, if the entity determines that it is more likely than not that a reporting unit's fair value is less than its carrying amount, a quantitative test is required.

Since the qualitative test is optional, an entity may decide to bypass the qualitative assessment and perform only the quantitative test, as discussed in Section 3.3, "Performing the quantitative goodwill impairment test." For example, entities may choose to bypass the qualitative test if the recent formal fair value measurement of a reporting unit was either very close to, or had a small margin above, the reporting unit's carrying amount. An entity may also choose to bypass the quantitative assessment if there are significant declines in macroeconomic, industry, and other market conditions or specific reporting unit changes, including declines in sales or changes in cost factors, overall financial performance, and reporting unit composition, as well as other relevant events and circumstances that affect the fair value or carrying amount of a reporting unit. When these types of significant factors or events are identified, an entity may reasonably conclude that the impact to the reporting unit's fair value is substantial enough that an entity should proceed directly to performing the quantitative test.

Figure 6 provides an overview of the annual impairment test considerations.

Figure 6: Annual impairment testing model for goodwill



The guidance in ASC 350-20-35-3C provides qualitative factors for an entity to consider when it elects to use the qualitative impairment assessment to determine whether it is more likely than not that goodwill is impaired and a quantitative impairment test is therefore required.

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

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 of 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).

While ASC 350-20-35-3C provides a list of events and circumstances to consider when determining whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount, that list is not all-inclusive. Entities should also consider other relevant events and circumstances that could affect the fair value or carrying amount of a reporting unit in determining whether a quantitative goodwill impairment test is necessary, as explained in ASC 350-20-35-3F and 35-3G.

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 quantitative 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 quantitative goodwill impairment test.

ASC 350-20-35-3G

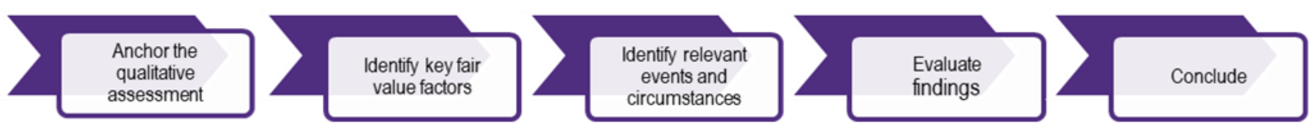
An entity shall evaluate, on the basis of the weight of evidence, the significance of all identified events and circumstances in the context of determining whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. None of the individual examples of events 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 quantitative 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 quantitative goodwill impairment test.

Once an entity has identified all of the positive and negative factors relevant to its qualitative assessment, it must weigh each factor according to its effect on either the reporting unit's fair value or its carrying amount. The entity must then assess the totality of all the identified events and circumstances and determine whether the reporting unit's fair value is more likely than not less than its carrying amount.

The main objective of the qualitative impairment assessment is to document the reporting entity's assessment of the events and circumstances that are used as inputs when formally estimating the fair value of the reporting unit and determining whether those events and circumstances, as of the date of the qualitative assessment, indicate that it is more likely than not that the fair value of the reporting unit is less than its carrying amount. Often this analysis takes the form of comparing how those events and circumstances have changed since the reporting entity last formally estimated the fair value of the reporting unit.

ASC 350 does not provide guidance on how to weigh various positive and negative factors. An entity may need to use significant judgment to perform this analysis. The existence of one negative event or factor does not automatically require an entity to perform a quantitative goodwill impairment test, and, likewise, the existence of a single mitigating event or positive factor does not overcome the need for the entity to perform a quantitative test.

The diagram below provides steps that may prove helpful when performing a qualitative assessment.



Step 1: Anchor the qualitative assessment

An entity may begin its qualitative assessment by "anchoring" that assessment to the margin between the reporting unit's most recent fair value estimate and its carrying amount. If the most recent fair value calculation shows that the reporting unit's fair value significantly exceeds its carrying amount, there is a larger amount of excess fair value that may be able to absorb fair value changes resulting from negative changes in events and circumstances, which could potentially impact the reporting unit's fair value.

An entity also should consider how much time has elapsed since the last fair value calculation. Generally, the more recently a fair value calculation was performed, the more likely that the entity can rely on that calculation as a basis for the qualitative assessment. Conversely, the more time that has elapsed since the last fair value calculation, the more challenging it will be to use that fair value calculation for the qualitative assessment. If a longer period of time has elapsed, it would be necessary to use more positive factors and events or circumstances to either indicate or support that it is not more likely than not that the fair value of the reporting unit is less than its carrying amount. Or, said another way, when a longer period of time has elapsed, more positive factors and events or circumstances would be necessary to support that it is not likely that goodwill is impaired and that a quantitative test would not be required. When a longer period of time has elapsed, it is more likely that an entity should bypass the qualitative assessment and perform a quantitative assessment. Many entities have an accounting policy stipulating that they will perform a quantitative test periodically to refresh the baseline fair value used when performing a qualitative test—for instance, at least every three years.

Step 2: Identify the main factors affecting fair value calculation

An entity should understand the key assumptions and significant inputs that drive the fair value calculation as part of its qualitative analysis. Since the objective of the qualitative impairment test is to evaluate whether it is more likely than not that the fair value of the reporting unit is less than its carrying amount, a significant component of a qualitative assessment is the identification of the key inputs used when estimating the reporting unit's fair value.

Step 3: Identify events and circumstances

An entity must determine whether any events or circumstances have occurred since the last quantitative impairment test that have an effect on the fair value of a reporting unit (see some examples outlined earlier in ASC 350-20-35-3C). Understanding the factors that most affect the fair value in Step 2 above will help an entity identify those events and circumstances impacting those factors. As part of its qualitative assessment, an entity must account for all the relevant events and circumstances that have occurred since the last time the reporting unit's fair value was formally determined.

Step 4: Evaluate findings

When performing a qualitative assessment, an entity must weigh all factors including the margin between the reporting unit's most recent fair value estimate and its carrying amount, key assumptions and significant inputs that drive the fair value estimate, and identified events and circumstances, and then evaluate them in totality to form a conclusion about whether it is more likely than not that a reporting unit's goodwill is impaired. While identifying those factors and events may be straightforward, the weighting of various factors requires a great deal of professional judgment. In general, greater weight is given to those factors that most affect fair value. An entity may also consider using a sensitivity analysis, such as updating the assumptions used in the prior year's fair value calculation, to help quantify which factors most affect fair value.

It is important to remember that no one factor is determinative. In addition to evaluating the significance of each negative factor, an entity should consider relevant positive and mitigating factors.

Step 5: Conclude on results

Once an entity has evaluated the identified events and circumstances, it must determine whether the results of a qualitative assessment indicate that it is more likely than not that a reporting unit's goodwill is impaired. If the entity concludes that goodwill is more likely than not impaired, the next step is to apply the quantitative test to calculate the impairment loss, if any.

Grant Thornton insight: Evaluation of qualitative impairment test factors

An entity is responsible for documenting the basis for its conclusions as part of its qualitative assessment of whether it is more likely than not that goodwill is impaired. In particular, an entity must document how it considered current events and circumstances that could affect the reporting unit's fair value or carrying amount. The nature and extent of the documentation may vary, depending upon the size and complexity of the entity and the nature of its goodwill, as well as on the amount of time that has elapsed since the last quantitative fair value calculation. Even though the assessment is qualitative in nature, management will often need to support its assessment with quantitative information, including the following:

- Key performance and economic indicators
- Market-dependent multiples and metrics
- Comparisons of budget to actual and prior-period amounts
- Cash flow analysis
- Foreign exchange rate fluctuations, if applicable

There is no prescribed method for performing a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount; however, the entity should take into consideration such factors as the following:

- *The difference between the carrying amount and the most recent quantitative fair value calculation* – The smaller the difference, the more likely it is that management will be required to perform a quantitative goodwill impairment test.
- *The time elapsed since the entity's last quantitative fair value calculation* – The more time that has elapsed since the last quantitative fair value calculation, the less relevant that fair value is likely to be, requiring more evidence to support management's qualitative assessment.
- *Identification and evaluation of all events and circumstances relevant to goodwill impairment:*
  - Consider the extent to which each event or circumstance could affect fair value.
  - Weight the events and circumstances that most affect fair value.
  - Consider positive and mitigating factors that may affect the more-likely-than-not determination.

The entity should support its assessment with sufficient evidence and documentation, and we believe that the entity should include appropriate and transparent disclosures about the qualitative assessment in the financial statements.

An entity should weigh the cost and benefits of performing a qualitative assessment compared to directly performing the quantitative impairment test. In certain circumstances, it may be beneficial to perform a qualitative assessment, such as when the fair value of the reporting unit significantly exceeded its carrying amount in a recent formal fair value measurement.

Grant Thornton insight: Consideration of recent quantitative fair value calculation

Under ASC 350-20-35-3F, if an entity has recently calculated the fair value of a reporting unit, it should consider the difference between that fair value amount and the reporting unit's carrying amount as a factor in its qualitative assessment to determine whether to perform a quantitative goodwill impairment test. By requiring an entity to consider a recent fair value measurement, the FASB is indicating that an entity may not ignore a previous fair value measurement in its qualitative assessment.

In addition, the relevance of a prior valuation of a reporting unit in an entity's qualitative assessment of goodwill impairment decreases over time. As more time elapses after the most recent measurement of a reporting unit's fair value, an entity should assign less weight to that fair value measurement as an input to its qualitative assessment. Therefore, to the extent that a prior fair value measurement provides evidence that goodwill is not impaired, that fair value measurement would become less relevant over time, and the reporting unit's qualitative assessment would rely more on other factors, such as macroeconomic conditions, industry and market conditions, cost factors, overall financial performance, changes in reporting unit composition, and other significant entity-specific changes. An entity might decide to forego the qualitative assessment when there is a high likelihood that a quantitative assessment will be required. The entity would then perform a quantitative fair value calculation.

As time passes, the relevance of a prior fair value calculation wanes, and so the strength of other qualitative factors will need to increase to compensate for a valuation that is more distant from the current annual impairment testing date. In practice, many entities have an accounting policy stipulating that they will perform a quantitative test periodically. However, such a policy does not remove the requirement to annually assess whether a quantitative test is needed based on the specific facts and circumstances.

Since there are no bright lines to evaluate when a new quantitative fair value calculation is required, significant judgment is needed when considering whether to rely on the most recent quantitative fair value calculation.

Conditions might indicate that goodwill is more likely than not impaired, including such factors as macroeconomic, industry, and market changes, as well as declining sales, increasing cost factors, declining overall financial performance, changes in reporting unit composition, or other factors, such as a small margin between the reporting unit's fair value and carrying amount in a recent fair value measurement. When these types of significant factors or events are identified, an entity may reasonably conclude that the impact to the reporting unit's fair value is substantial enough that an entity should proceed directly to performing the quantitative test and forego performing a qualitative test. Section 3.3, "Performing the quantitative goodwill impairment test," discusses the quantitative test for goodwill impairment.

Qualitative assessment is optional

An entity is not required to perform the qualitative assessment and may proceed directly to the quantitative test for goodwill impairment without evaluating any of the factors listed in ASC 350-20-35-3C. In addition, an entity is not required to make a policy election regarding how it evaluates goodwill for impairment on an annual basis. In other words, an entity may take a qualitative approach one year and may choose to perform a quantitative test directly the next year without making a qualitative assessment.

An entity with more than one reporting unit may utilize a mix of qualitative assessments and quantitative tests among its reporting units.

Considerations when using the qualitative approach

An entity executes a business combination, recognizes goodwill as of January 1, 20X1, and sets the annual goodwill impairment testing date as of October 1. The acquired business constitutes a single reporting unit. The entity has a policy of performing a quantitative fair value impairment test at least every three years. On October 1, 20X1 and 20X2, the entity decides to perform a qualitative assessment, using the quantitative fair value calculation associated with the acquisition as an input for that reporting unit's assessment.

However, for the October 1, 20X3 evaluation, the entity determines that it might have a difficult time using the January 1, 20X1 fair value of the reporting unit as an input in the qualitative assessment because prior valuations lose relevance over time. The entity concludes that facts and circumstances indicate that the passage of nearly three years has rendered the prior valuation significantly less relevant in the current circumstances and proceeds directly to performing the quantitative test for goodwill impairment.

Conversely, if the entity evaluates the events and circumstances at October 1, 20X3 and determines there is strong enough evidence to support a conclusion that goodwill is not more likely than not impaired, it may perform a qualitative test. The results of that assessment would determine whether the entity should also perform a quantitative test.

Reporting units with zero or negative carrying amounts

The amendments in ASU 2017-04 eliminated Step 2 of the quantitative goodwill impairment test in ASC 350. Prior to the adoption of these amendments, and as discussed in Paragraphs 35 and 36 in the ASU's Basis for Conclusions (BC35 and BC36), an entity was required to perform a qualitative assessment to determine whether it was more likely than not that goodwill was impaired for reporting units with net assets that had a zero or negative carrying amount. If the qualitative test revealed that it was more likely than not that impairment existed, an entity was then required to perform the Step 2 quantitative test. Although the amendments in ASU 2017-04 do not provide specific guidance for calculating goodwill impairment when a reporting unit has a zero or negative carrying amount, the FASB acknowledged in BC36 that goodwill impairment would be unlikely, since the fair value of a reporting unit with a zero or negative carrying amount is likely to exceed its carrying amount. An entity is still required under the amendments to disclose the amount of goodwill allocated to reporting units with zero or negative carrying amounts, along with the reportable segment that includes that reporting unit, as discussed in ASC 350-20-50-1A.

ASC 350-20-50-1A

Entities that have one or more reporting units with zero or negative carrying amounts of net assets shall disclose those reporting units with allocated goodwill and the amount of goodwill allocated to each and in which reportable segment the reporting unit is included.

3.2.3 Other circumstances requiring impairment testing

There are other circumstances in which an impairment test of goodwill may be required in addition to the annual impairment test and the interim impairment test when a triggering event is identified (see Section 3.2.4, “Interim impairment considerations”), such as when a portion of a reporting unit is disposed of, reporting unit determinations have changed, or the reporting units are reorganized.

Disposal of a portion of a reporting unit

If an entity disposes of part of a reporting unit and the disposal group constitutes a “business,” as defined in ASC 805, the entity must allocate a portion of any goodwill assigned to that reporting unit to the carrying amount of the disposed business to determine the gain or loss upon disposal. The amount of goodwill allocated to the disposed business is based on the relative fair values of the disposed business and the retained portion of the reporting unit on an individual, stand-alone basis, as indicated in ASC 350-20-40-1 to 40-6, unless goodwill related to the disposed business was never integrated into the reporting unit’s operations after being acquired. Situations in which the acquired entity operates as a stand-alone entity are expected to be infrequent, since some degree of integration into the acquirer’s reporting unit or units generally occurs after an acquisition.

ASC 350-20-40-1

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.

ASC 350-20-40-2

When a portion of a reporting unit that constitutes a business (see Section 805-10-55) or nonprofit activity is to be disposed of, goodwill associated with that business or nonprofit activity shall be included in the carrying amount of the business or nonprofit activity in determining the gain or loss on disposal.

ASC 350-20-40-3

The amount of goodwill to be included in that carrying amount shall be based on the relative fair values of the business or nonprofit activity to be disposed of and the portion of the reporting unit that will be retained. For example, if a reporting unit with a fair value of $400 is selling a business or nonprofit activity for $100 and the fair value of the reporting unit excluding the business or nonprofit activity being sold is $300, 25 percent of the goodwill residing in the reporting unit would be included in the carrying amount of the business or nonprofit activity to be sold.

ASC 350-20-40-4

However, if the business or nonprofit activity 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 or nonprofit activity to be disposed of.

ASC 350-20-40-5

That situation might occur when the acquired business or nonprofit activity is operated as a standalone entity or when the business or nonprofit activity is to be disposed of shortly after it is acquired.

ASC 350-20-40-6

Situations in which the acquired business or nonprofit activity is operated as a standalone entity are expected to be infrequent because some amount of integration generally occurs after an acquisition.

The following example shows how to allocate goodwill when only a portion of a reporting unit is disposed of.

Allocation of goodwill when disposing of a portion of a reporting unit

Entity A, which has three reporting units, sells a portion of reporting unit 3 to Entity B. Before the sale, reporting unit 3 consists of two business operations and the portion of reporting unit 3 being sold represents a "business" based on the guidance in ASC 805.

The fair value of reporting unit 3 prior to the sale of one of its business operations to Entity B is $1,500. The fair value amount includes a portion of its value from the synergies between reporting unit 3's two businesses. The stand-alone fair value of the portion of the reporting unit being sold is $400, and the stand-alone fair value of the portion of the reporting unit being retained is $800 (that is, the fair values of the two business operations comprising reporting unit 3, without considering the synergies between the two businesses). Based on the stand-alone fair values of the portions of reporting unit 3 being sold and being retained, Entity A would allocate 33 percent ($400 ÷ [$400 + $800]) of the goodwill in reporting unit 3 to the carrying amount of the business being sold to Entity B for purposes of determining the gain or loss on disposal.

Grant Thornton insight: Synergy considerations when allocating goodwill to a disposal

Entities need to exercise caution when considering the amount of goodwill to be allocated to a disposal when synergies between operations exist. In the previous example, it would not be appropriate to allocate 27 percent ($400 ÷ $1,500) of the reporting unit's goodwill to the carrying amount of the disposed component business operation. It also would not be appropriate to use the $1,500 fair value of the reporting unit in the allocation calculation, because it includes the synergies of operating both of reporting unit 3's business operations together and would not therefore represent the individual fair values of the two separate business operations within reporting unit 3.

ASC 350-20-40-8 and 40-9 provide specific guidance on accounting for a disposal of a portion of a reporting unit for nonpublic entities using the accounting alternative for amortizing goodwill in ASC 350-20-35-63 to 35-64 (see Section 4.1, "Amortization of goodwill accounting alternative," for a detailed discussion of the private company alternative).

Grant Thornton insight: Goodwill impairment testing considerations when disposing of a portion of a reporting unit

We believe that an entity should assess goodwill attributed to the combined reporting unit for impairment immediately before allocating a portion of a reporting unit's goodwill to a disposed group that constitutes a business. According to the guidance in ASC 350-20-35-3C(f), the disposal of a portion or all of a reporting unit creates a more-likely-than-not indicator that goodwill could be impaired, so that an entity should perform an impairment test before it allocates goodwill between the portion of the reporting unit being retained and the portion being disposed of. A failure to recognize an impairment that exists in goodwill prior to the disposition could result in a misstatement in the gain or loss from the sale of the disposed group.

An entity should perform a goodwill impairment test immediately after reallocating goodwill for the portion of the reporting unit retained as a result of a disposal, as indicated in ASC 350-20-40-7. Testing goodwill in the reporting unit for impairment before and after the reallocation identifies any goodwill impairment that could otherwise be concealed by the disposal.

ASC 350-20-40-7

When only a portion of goodwill is allocated to a business or nonprofit activity 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 paragraphs 350-20-35-3A through 35-19 using its adjusted carrying amount.

Change or reorganization of reporting unit structure

In our view, an entity would generally be expected to test goodwill for impairment immediately before and after a reorganization or other event that results in a change to an entity's reporting units. ASC 350-20-35-45 and 35-46 provide guidance on allocating goodwill between reporting units affected by a reorganization of an entity's reporting structure. In a reorganization event, an entity's assets and liabilities, including goodwill, are reassigned to the reporting units affected using a relative fair value method. The impairment testing and reallocation of goodwill is similar to accounting for a disposal of a portion of a reporting unit, as discussed above in "Disposal of a portion of a reporting unit."

ASC 350-20-35-45

When an entity reorganizes its reporting structure in a manner that changes the composition of one or more of its reporting units, the guidance in paragraphs 350-20-35-39 through 35-40 shall be used to reassign assets and liabilities to the reporting units affected. However, goodwill shall be reassigned to the reporting units affected using a relative fair value allocation approach similar to that used when a portion of a reporting unit is to be disposed of (see paragraphs 350-20-40-1 through 40-7).

ASC 350-20-35-46

For example, if existing reporting unit A is to be integrated with reporting units B, C, and D, goodwill in reporting unit A would be assigned to units B, C, and D based on the relative fair values of the three portions of reporting unit A prior to those portions being integrated with reporting units B, C, and D.

The following example illustrates the allocation of goodwill to reporting units in a reorganization of an entity's reporting units.

Reorganization of reporting units with goodwill reassigned to a new reporting unit

APG Corp. has two reporting units (RU), RU-1 and RU-2. APG Corp. reorganizes its reporting structure during the current reporting period and, as part of that reorganization process, transfers portions of the legacy reporting units into a newly formed reporting unit, RU-3. Amounts prior to the reorganization are as shown in the following table.

(Amounts in 000's)	RU-1	RU-2	Total
Fair value of RU	$ 60,000	$ 100,000	$ 160,000
Goodwill	20,000	70,000	90,000
Fair value – transferred portion	30,000	10,000	40,000
Relative fair value transferred	50%	10%	

As noted in ASC 350-20-35-45 and 35-46, goodwill must be reassigned among the three reporting units based on the relative fair value of the portions of the reporting units that are reassigned. Upon reorganization, assignment of goodwill to RU-3 is shown in the following table.

(Amounts in 000's)	RU-1	RU-2	Total
Original goodwill	$ 20,000	$ 70,000	$ 90,000
Relative fair value transferred	50%	10%	
Goodwill assigned to RU-3	10,000	7,000	17,000

The following table shows the goodwill in each reporting unit after the reorganization.

(Amounts in 000's)	RU-1	RU-2	RU-3	Total
Fair value of RU	$30,000	$90,000	$40,000	$160,000
Original goodwill	$20,000	$70,000	$ -	$ 90,000
Goodwill assigned to RU-3	(10,000)	(7,000)	17,000	-
Reallocated goodwill	$10,000	$63,000	$17,000	$ 90,000

3.2.4 Interim impairment considerations

The guidance in ASC 350-20 requires an entity to monitor and evaluate triggering events—those events or circumstances that make it more likely than not that a reporting unit's fair value is less than its carrying amount—throughout the fiscal year in between annual impairment tests. When a triggering event occurs, the entity must then test goodwill for impairment by performing a quantitative impairment test in accordance with ASC 350-20-35-4, as discussed in Section 3.3, "Performing the quantitative goodwill impairment test."

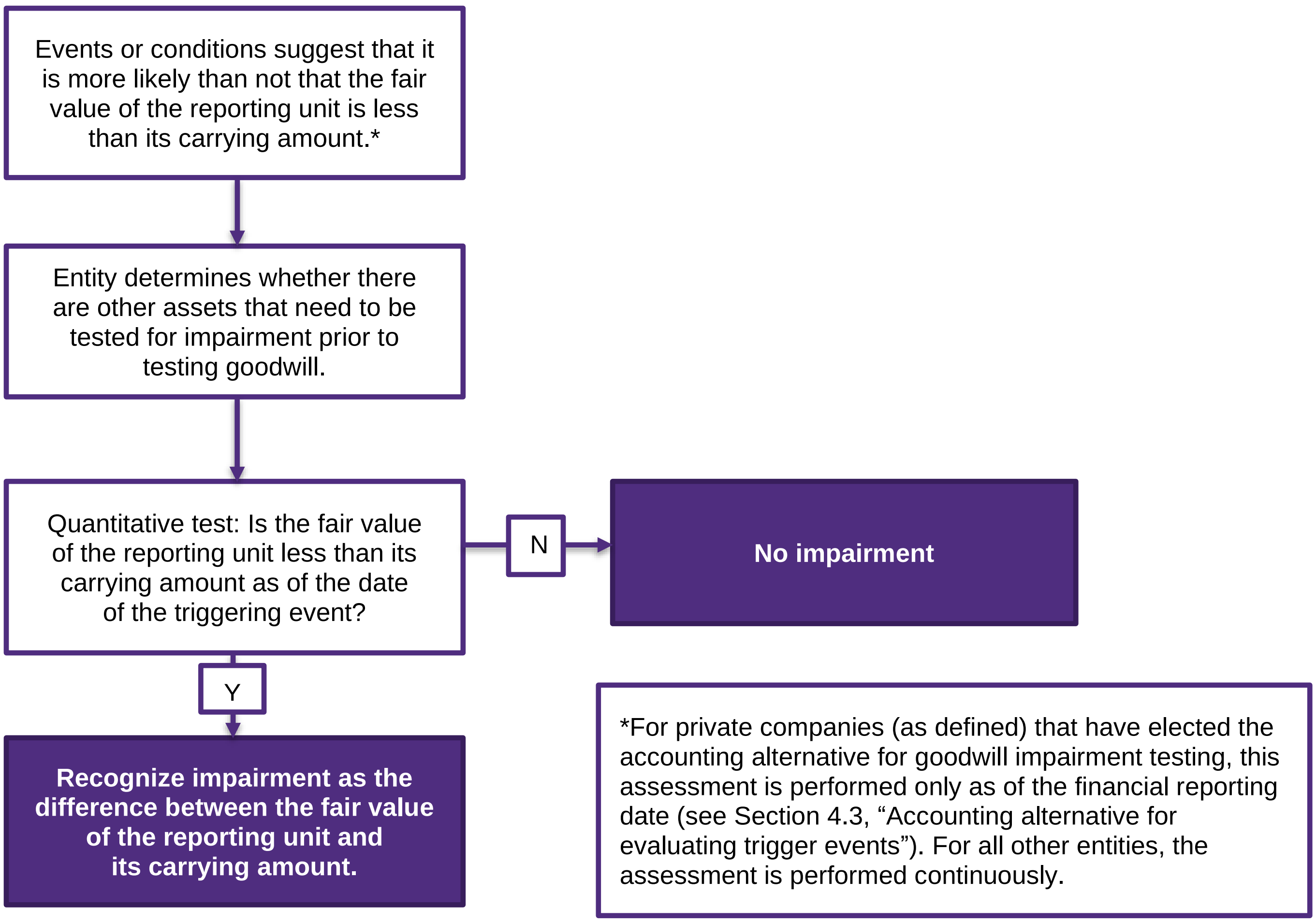
Grant Thornton insight: Triggering events

The date of a triggering event is the date when circumstances first indicate that it is more likely than not that the fair value of the reporting unit is less than its carrying amount. A triggering event also might not be a single event or circumstance, but could instead be an aggregation or accumulation of events and circumstances that lead to a conclusion that it is more likely than not that the fair value of the reporting unit is less than its carrying amount.

When a triggering event is identified, an entity must perform an impairment test as of the triggering event date, using only the known events and circumstances as of that date. In order to perform the impairment test (that is, to determine whether the fair value of the reporting unit exceeds its carrying amount) similar to an annual impairment test date that might not be at the end of a reporting period, the entity must effectively "close its books" as of the triggering event date to appropriately determine the carrying amount of the reporting unit and then perform its impairment test as of that date, even though the triggering event date may not be the end of a reporting period when the entity typically "closes its books."

Figure 7 provides an overview of the interim impairment testing model for goodwill between annual impairment tests.

Figure 7: Interim impairment testing model for goodwill



ASC 350-20-35-30

Goodwill 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. Paragraphs 350-20-35-3F through 35-3G describe the process for making these evaluations.

The factors described in ASC 350-20-35-3C that are used in the qualitative impairment test are the same factors used to determine whether goodwill must be tested for impairment between annual tests. When these factors indicate that it is more likely than not that the fair value of a reporting unit is below its carrying amount, the entity should perform the quantitative goodwill impairment test. Similar to the guidance for indefinite-lived intangible assets, the date of the triggering event is the date used to perform the goodwill impairment test, except for private entities that have adopted the practical expedient to test for impairment at the end of the reporting period, as discussed in Section 4.3, “Accounting alternative for evaluating triggering events.”

Paragraphs (a) through (g) in ASC 350-20-35-3C include several examples of factors that might indicate that a reporting unit’s fair value is more likely than not less than its carrying amount. Some events and circumstances that an entity should consider include the following:

- Macroeconomic conditions, such as
  a. Deterioration in general economic conditions
  b. Limited access to capital
  c. Variations in foreign exchange rates
  d. Other developments in equity and credit markets
- Industry and market considerations, such as
  a. Deterioration in the entity’s operating environment
  b. Increased competition
  c. Decline in market-independent multiples or metrics, both in general and relative to peers
  d. Market changes for the entity’s products or services
  e. Regulatory or political developments
- Cost factors, such as increases in the cost of raw materials or labor that would negatively impact earnings and cash flows
- Overall financial performance, such as
  a. Negative or declining cash flows
  b. Decline in actual or expected revenue and earnings compared to actual and projected results of relevant prior periods
- Reporting unit events, such as
  a. Change in composition or carrying amount of net assets
  b. More-likely-than-not expectation of selling or disposing of all or a portion of a reporting unit
  c. Test for recoverability of a significant asset group within a reporting unit
  d. Recognition of a goodwill impairment loss in the financial statements of a subsidiary that is a component of a reporting unit
- Sustained decrease in share price (considered in both absolute terms and relative to peers)
- Other relevant entity-specific events, such as
  a. Changes in management, key personnel, strategy, or customers
  b. Contemplation of bankruptcy
  c. Litigation

At the 2008 AICPA National Conference on Current SEC and PCAOB Developments, the SEC staff outlined some additional examples of events and circumstances that could trigger a goodwill impairment test in between an entity's annual testing dates, including the following:

- The impairment of other assets or an increase in valuation allowances
- Cash or operating losses of a reporting unit
- Weak industry outlook
- Missed analyst expectations or revised downward forecasts
- Plans to restructure operations, including layoffs and store closings
- Reorganization of reporting units
- Declines in market capitalization below book value

The factors listed above are not all-inclusive, and an entity should consider all relevant events and circumstances that could affect whether it is more likely than not that a reporting unit's fair value is less than its carrying amount.

Share price and market capitalization decline as an indicator for impairment

For public entities, a drop in share price resulting in a decline in market capitalization might be an indicator of impairment. At the 2008 AICPA National Conference on Current SEC and PCAOB Developments, the SEC staff reported that public entities should consider the reasons underlying a drop in share price and determine whether an impairment triggering event has occurred. Although the staff recognizes that the volatility of global capital markets might cause market capitalization to fall below book value and such a drop might not be an impairment triggering event, the staff still expects registrants in these situations to fully evaluate such deficiencies.

Comparing a drop in share price to decreases in general indices could provide meaningful insight for purposes of such an evaluation. For example, a share price that drops below market trends may be an indicator of an impairment trigger for the entity. An entity also needs to consider whether a drop in share price consistent with a drop in market trends indicates that there is a triggering event, as the whole market has lost value. In addition, public companies should consider how their share price has been impacted by general market conditions and volatility. For some companies, short-term spikes or short sales might have a significant impact on fair value, but the SEC staff cautions entities to distinguish between short-term spikes and routine trading activity, taking into consideration such factors as the duration and severity of the share price decline. Large deviations between book value and market capitalization will increase the staff's skepticism when evaluating a registrant's conclusion that an interim goodwill impairment test was not necessary. In other words, the staff indicated that it is not appropriate to assume that a drop in market price is temporary without examining the underlying reasons to support such a conclusion.

Grant Thornton insight: SEC comment letters on market capitalization declines

The SEC staff might issue a comment letter to a registrant in situations where book value exceeds market capitalization and the registrant does not record a goodwill impairment charge or disclose that it performed an interim impairment analysis. These comments might include requests for registrants to disclose the basis for concluding that an interim analysis or impairment charge was not deemed necessary.

Registrants are also reminded to consider market capitalization when markets in general show improvements and when a registrant's own market capitalization has changed in a direction that differs from the markets' direction.

Testing considerations for recently acquired goodwill

Questions often arise about the proper timing of an initial impairment test for goodwill after an entity acquires another entity. There is no specific guidance that requires an entity to test goodwill for impairment on the date of acquisition.

Grant Thornton insight: Goodwill impairment test dates for acquisitions

Although there is no requirement to test goodwill for impairment on the date of acquisition, Paragraph 382 in the Basis for Conclusions of Statement of Financial Accounting Standards 141(R) suggests that an entity should test goodwill for impairment if impairment indicators exist:

> The Boards [FASB and IASB] acknowledged that overpayments are possible, in concept, and overpayment should lead to the acquirer's recognition of an expense (or loss) in the period of the acquisition. However, the Boards believe that in practice any overpayment is unlikely to be detectable or known at the acquisition date. That is, the Boards are not aware of instances in which a buyer knowingly overpays or is compelled to overpay a seller to acquire a business. Even if an acquirer thinks it might have overpaid in some sense, the amount of overpayment would be difficult, if not impossible, to quantify. Thus, the Boards concluded that in practice it is not possible to identify and reliably measure an overpayment at the acquisition date. Accounting for overpayments is best addressed through subsequent impairment testing when evidence of a potential overpayment first arises.

Accordingly, we believe that entities should test goodwill for impairment if impairment indicators exist, without regard to how recently the goodwill was recognized or whether the accounting for a business combination is still being finalized.

The guidance in ASC 350-20-35-28 requires goodwill to be tested for impairment at least annually. The initial goodwill impairment test related to an acquisition should occur within 12 months of the acquisition date, unless one of the triggering events outlined in ASC 350-20-35-3C occurs, requiring an earlier test. Whether the annual test should be performed in the fiscal year of an acquisition depends on both the acquisition date and the annual impairment testing date. If, for example, the annual goodwill impairment test date follows shortly after the acquisition, a goodwill impairment test should be performed on that annual testing date. Conversely, if the annual goodwill impairment test date occurs shortly before the acquisition, an entity could wait to perform a goodwill impairment test for the acquired goodwill until the next annual goodwill impairment test date (assuming that no impairment triggers occur before the next annual goodwill impairment test date). When the annual goodwill impairment test occurs shortly before the acquired goodwill is recognized, more than one year may not elapse between the acquisition of the goodwill and the performance of the next annual goodwill impairment test.

The example below provides considerations for determining whether the annual impairment test should be performed for an acquired entity's goodwill.

Timing of annual goodwill impairment test for a recent acquisition

Entity A has a calendar year-end and acquires Entity B on November 1, 20X0, which results in a new reporting unit for Entity A. If Entity A determines that October 1 is the new reporting unit's annual goodwill impairment testing date, it would not be required to perform an annual impairment test in 20X0, because the next annual impairment testing date of October 1, 20X1 falls within 12 months of the acquisition date.

If Entity A determines that December 1 is the annual goodwill impairment testing date for the new reporting unit, then the initial goodwill impairment test should be performed on December 1, 20X0, since the next annual impairment test date of December 1, 20X1 exceeds the permitted time frame of 12 months after the acquisition date.

Grant Thornton insight: Newly acquired goodwill and the qualitative impairment test

If no quantitative goodwill impairment test has yet been performed for a recently acquired entity's reporting unit, questions may arise as to whether it is appropriate to perform a qualitative annual goodwill impairment test to determine whether a quantitative annual goodwill impairment test is necessary. While management may assess and document the reasons why a qualitative assessment may or may not be appropriate based on its circumstances, the starting point for a qualitative analysis would include the length of time since the acquisition and the likelihood that the reporting unit's fair value is less than its carrying amount. The evidence for a qualitative assessment would still need to support that it is not more likely than not that the fair value of the reporting unit is less than its carrying amount.

Use of a valuation specialist may be necessary to assist with identifying the inputs that are most impactful to a quantitative fair value calculation in determining the appropriateness of a qualitative assessment after a recent acquisition.

3.3 Performing the quantitative goodwill impairment test

When an entity determines that a quantitative impairment test is required, it should compare the reporting unit's fair value to its carrying amount. Impairment is recognized to the extent that the carrying amount of a reporting unit(s) exceeds the fair value of the reporting unit(s), not to exceed the total amount of goodwill allocated to the reporting unit(s). Accordingly, an entity needs a well-designed and controlled process to determine the carrying amount and fair value of its reporting units in order to appropriately perform a quantitative goodwill impairment test.

ASC 350-20-35-4

The quantitative goodwill impairment test, used to identify both the existence of impairment and the amount of impairment loss, compares the fair value of a reporting unit with its carrying amount, including goodwill.

ASC 350-20-35-5

The guidance in paragraphs 350-20-35-22 through 35-24 shall be considered in determining the fair value of a reporting unit.

ASC 350-20-35-6

If the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not impaired.

ASC 350-20-35-8

If the carrying amount of a reporting unit exceeds its fair value, an impairment loss shall be recognized in an amount equal to that excess, limited to the total amount of goodwill allocated to that reporting unit. Additionally, an entity shall consider the income tax effect from any tax deductible goodwill on the carrying amount of the reporting unit, if applicable, in accordance with paragraph 350-20-35-8B when measuring the goodwill impairment loss

3.3.1 Determining reporting unit's carrying amount

When determining the carrying amount of a reporting unit, an entity should assign goodwill from business acquisitions and allocate assets and liabilities, including deferred income taxes, to the appropriate reporting unit(s).

In addition to allocating assets and liabilities to the appropriate reporting units when acquired or upon a change in segments, critical to the process of determining the carrying amount of a reporting unit each period before performing a goodwill impairment test is first performing any other necessary impairment tests on the allocated assets (other than goodwill), as discussed in Section 1. Performing an impairment test first on the reporting unit assets (other than goodwill) is important because the carrying amount of the reporting units would be impacted by any asset impairment recognized as a result of other impairment tests performed before the goodwill impairment test.

The following sections discuss allocating assets and liabilities and assigning goodwill to reporting units for purposes of determining the carrying amount of a reporting unit.

Allocating assets and liabilities to reporting units

Assets and liabilities must be assigned to reporting units to determine the appropriate carrying amount of a reporting unit for purposes of performing a goodwill impairment test. However, reporting units may be determined based only on financial information that is included in the income statement provided to the chief operating decision maker when the operating segment is the reporting unit, or to the segment manager when a reporting unit is a level below an operating segment, while all of the assets and liabilities (other than goodwill) might not yet have been assigned to the reporting unit.

Accordingly, an entity with more than one reporting unit may need to establish a reasonable and consistent process to assign assets and liabilities to reporting units when a business combination or asset acquisition occurs, similar to its process for allocating goodwill. The guidance in ASC 350-20-35-39 describes two criteria that must both be met for an asset or liability to be assigned to a reporting unit for impairment testing. When allocating assets and liabilities to reporting units for the goodwill impairment test, the main objective, according to ASC 350-20-35-39, is to ensure that the entity includes in the reporting unit's carrying amount only those assets or liabilities that are both (1) generating the reporting unit's cash flows, and (2) being used in determining the unit's fair value.

ASC 350-20-35-39

For the purpose of testing goodwill for impairment, acquired assets and assumed liabilities shall be assigned to a reporting unit as of the acquisition date if both of the following criteria are met:

a. The asset will be employed in or the liability relates to the operations of a reporting unit.

b. The asset or liability will be considered in determining the fair value of the reporting unit.

Assets or liabilities that an entity considers part of its corporate assets or liabilities shall also be assigned to a reporting unit if both of the preceding criteria are met. Examples of corporate items that may meet those criteria and therefore would be assigned to a reporting unit are environmental liabilities that relate to an existing operating facility of the reporting unit and a pension obligation that would be included in the determination of the fair value of the reporting unit. This provision applies to assets acquired and liabilities assumed in a business combination and to those acquired or assumed individually or with a group of other assets.

ASC 350-20-35-40

Some assets or liabilities may be employed in or relate to the operations of multiple reporting units. The methodology used to determine the amount of those assets or liabilities to assign to a reporting unit shall be reasonable and supportable and shall be applied in a consistent manner. For example, assets and liabilities not directly related to a specific reporting unit, but from which the reporting unit benefits, could be assigned according to the benefit received by the different reporting units (or based on the relative fair values of the different reporting units). In the case of pension items, for example, a pro rata assignment based on payroll expense might be used. A reasonable allocation method may be very general. For use in making those assignments, the basis for and method of determining the fair value of the acquiree and other related factors (such as the underlying reasons for the acquisition and management's expectations related to dilution, synergies, and other financial measurements) shall be documented at the acquisition date.

ASC 350-20 does not explicitly address whether or not an entity with only one reporting unit should assign all of its assets and liabilities to that reporting unit. However, the FASB's EITF Agenda Committee indicated in 2002 that an entity with only one reporting unit should assign all of its assets and liabilities to that reporting unit.

Although ASC 350-20 does not require an entity to assign all assets and liabilities acquired to reporting units, the guidance does indicate that any corporate assets or liabilities that meet both criteria in ASC 350-20-35-39 should be assigned to a reporting unit, including environmental liabilities that relate to an existing operating facility and pension obligations, as they are included in determining a reporting unit's fair value. Entities are not required to assign corporate assets and liabilities that do not meet both of the criteria established in ASC 350-20-35-39 to a reporting unit. For example, an entity would not be required to assign a building that is not used by the entity's individual reporting units to those individual reporting units, or a corporate warranty liability that relates to a product produced by a reporting unit that was sold and is no longer being produced by the entity's remaining reporting units.

Grant Thornton insight: Assigning assets, liabilities, and goodwill to reporting units

The methodology used to determine the assets and liabilities assigned to a reporting unit should be reasonable and supportable and applied in a consistent manner. Significant judgment will be necessary when an asset or liability is either used by or relates to the operations of more than one reporting unit, and an entity is forced to allocate amounts. Entities may require assistance from third-party valuation experts when assigning assets, liabilities, and goodwill to reporting units when allocations are determined to be based upon, for example, relative fair values of the reporting units or discounted cash flows related to usage of an asset. Entities should maintain documentation of reporting unit assignments, including the basis and the methodology used for each assignment, and consistently apply the same methodology, similar to any other accounting principle.

Assigning goodwill to reporting units

An entity should assign goodwill to one or more reporting units when goodwill is initially recognized. Goodwill should be assigned to the reporting units that are expected to benefit from the synergies of the business combination, even if the acquired assets and assumed liabilities are not assigned to that reporting unit. "Synergy" is an interaction where the combined value and performance of two separate business operations is greater than the sum of the individual operations alone, yielding a potentially enhanced financial benefit, such as enhanced cash flows or reduced operational risks. The amount of goodwill allocated to each reporting unit should be determined in a reasonable and supportable manner, and the method(s) used to allocate goodwill to reporting units should be applied consistently. The guidance in ASC 350-20-35-42 through 35-43 describes the acquisition method and the with-and-without method, which are both commonly used to assign goodwill to reporting units.

Acquisition method

When a reporting unit is expected to benefit from the synergies of an acquisition and a portion of the acquired business is assigned to the reporting unit, the acquisition method for assigning goodwill to the reporting would generally be appropriate. The acquisition method follows an approach similar to the approach used to allocate the purchase price and determine the amount of goodwill in a business combination. The fair value of the portion of the acquired business assigned to the reporting unit is compared to the aggregate fair value of the individual assets and liabilities assigned to that reporting unit, with the difference being the amount of goodwill assigned to the reporting unit.

With-and-without method

If the acquired assets and liabilities are assigned to a single reporting unit and another reporting unit is also expected to benefit from those assets and liabilities, an entity would generally use the with-and-without method to allocate goodwill to all reporting unit(s) that are expected to benefit from the acquisition synergies. When applying the with-and-without method, the difference between the fair value of the reporting unit before the acquisition and its fair value after the acquisition is the amount of goodwill that is assigned to the reporting unit.

We believe that when the with-and-without method provides a more reasonable and supportable assignment of goodwill, based on how an entity's reporting units are expected to benefit from the synergies of an acquisition, this method of allocating goodwill could also be used to assign goodwill to a reporting unit that has other assets and liabilities assigned to it, if those reporting units also benefit from the synergies of an acquisition similarly to a reporting unit that has not been assigned any of the assets acquired or liabilities assumed, as indicated in ASC 350-20-35-43.

ASC 350-20-35-41

For the purpose of testing goodwill for impairment, all goodwill acquired in a business combination shall be assigned to one or more reporting units as of the acquisition date. Goodwill shall be assigned to reporting units of the acquiring entity that are expected to benefit from the synergies of the combination even though other assets or liabilities of the acquired entity may not be assigned to that reporting unit. The total amount of acquired goodwill may be divided among a number of reporting units. The methodology used to determine the amount of goodwill to assign to a reporting unit shall be reasonable and supportable and shall be applied in a consistent manner. In addition, that methodology shall be consistent with the objectives of the process of assigning goodwill to reporting units described in paragraphs 350-20-35-42 through 43.

ASC 350-20-35-42

In concept, the amount of goodwill assigned to a reporting unit would be determined in a manner similar to how the amount of goodwill recognized in a business combination is determined. That is:

a. An entity would determine the fair value of the acquired business (or portion thereof) to be included in a reporting unit—the fair value of the individual assets acquired and liabilities assumed that are assigned to the reporting unit. Subtopic 805-20 provides guidance on assigning the fair value of the acquiree to the assets acquired and liabilities assumed in a business combination.

b. Any excess of the fair value of the acquired business (or portion thereof) over the fair value of the individual assets acquired and liabilities assumed that are assigned to the reporting unit is the amount of goodwill assigned to that reporting unit.

ASC 350-20-35-43

If goodwill is to be assigned to a reporting unit that has not been assigned any of the assets acquired or liabilities assumed in that acquisition, the amount of goodwill to be assigned to that unit might be determined by applying a with-and-without computation. That is, the difference between the fair value of that reporting unit before the acquisition and its fair value after the acquisition represents the amount of goodwill to be assigned to that reporting unit.

ASC 350-20-35-44

This Subtopic does not require that goodwill and all other related assets and liabilities assigned to reporting units for purposes of testing goodwill for impairment be reflected in the entity's reported segments. However, even though an asset may not be included in reported segment assets, the asset (or liability) shall be allocated to a reporting unit for purposes of testing for impairment if it meets the criteria in paragraph 350-20-35-39.

The following examples show how to allocate goodwill to more than one reporting unit using both the acquisition method and the with-and-without method when net assets and goodwill from an acquisition are assigned to reporting units that already have assets and liabilities assigned to them.

Allocating goodwill to reporting units

APG Corp. acquires Target Co. for $100 million. At the acquisition date, APG Corp. determines that Target Co. has $10 million of net working capital, $60 million of identifiable tangible and intangible assets, and $30 million of goodwill.

Prior to the acquisition, APG Corp. determines that it has two reporting units (RU): RU-1 and RU-2. After the acquisition, Target Co. is integrated into both of these reporting units. The allocation of the identifiable net assets of Target Co. between RU-1 and RU-2 is shown in the following table.

(amounts in 000's)	RU-1	RU-2	Total
Net working capital	$ 7	$ 3	$10
Tangible and intangible assets	40	20	60
Net assets assigned to reporting unit	$47	$23	$70

Acquisition method

Under the acquisition method, APG Corp. assigns the goodwill of the acquired business to APG's two reporting units based on the difference between the fair value of the acquired business's identifiable net assets that are assigned to each reporting unit, and the fair value of the portion of the acquired business that is assigned to the reporting unit. This example assumes that the fair value of the portion of the acquired business assigned to each reporting unit equals the pro rata share (based on net identifiable assets) of the total purchase price of the acquired business.

(amounts in 000's)	RU-1	RU-2	Total
Fair value of acquired business (or portion of)	$70	$30	$100
Less: Fair value of net assets to be assigned (see first table)	(47)	(23)	(70)
Goodwill assigned to reporting units	$23	$ 7	$30

With-and-without method

Under the with-and-without method, APG Corp. assigns goodwill between the two reporting units based on the difference between (1) the fair value of the net assets of the reporting unit after the acquisition, and (2) the fair value of the reporting unit before the acquisition.

The following table shows how APG Corp. determines the goodwill to assign to the reporting units using the with-and-without method.

(amounts in 000's)	RU-1	RU-2	Total
Fair value of reporting unit – after acquisition	$100	$115	$215
Less: fair value of reporting unit – prior to acquisition	(30)	(85)	(115)
Fair value of acquired business or asset group	70	30	100
Less: fair value of net assets to be assigned (per above)	(47)	(23)	(70)
Goodwill assigned to reporting unit	$23	$7	$30

Allocating deferred income taxes to reporting units

When determining the carrying amount of a reporting unit for the purpose of performing the goodwill impairment test, deferred income taxes should be included in the carrying amount of the reporting unit regardless of whether the fair value of the reporting unit is determined, assuming the unit will be sold in a taxable or nontaxable transaction, as described in ASC 350-20-35-7. Any deferred tax assets and liabilities resulting from book to tax basis differences related to assets and liabilities assigned to a reporting unit should also be assigned to the related reporting unit(s).

ASC 350-20-35-7

In determining the carrying amount of a reporting unit, deferred income taxes shall be included in the carrying amount of the reporting unit, regardless of whether the fair value of the reporting unit will be determined assuming it would be bought or sold in a taxable or nontaxable transaction.

Grant Thornton insight: Allocating valuation allowances to reporting units

When allocating deferred tax assets and liabilities to reporting units, questions can arise related to whether valuation allowances should also be allocated to the reporting units. We believe that valuation allowances would be considered part of the deferred tax assets for the reporting unit(s) and should also be included in the carrying amount of the reporting unit(s).

3.3.2 Determining the fair value of reporting unit

Determining the fair value of the reporting unit(s) is also a key step in performing a quantitative goodwill impairment test.

The fair value of a reporting unit is the price that a reporting unit would realize in an orderly sale in the current market (not a forced or liquidation sale value) at the fair value measurement date. A quoted market price in an active market is the best evidence of fair value and should be used if available. When a quoted market price is unavailable, an entity should estimate the fair value. An entity may use any valuation model consistent with fair value concepts when estimating the fair value of a reporting unit for the goodwill impairment test, as noted in ASC 350-20-35-22 and 35-24.

ASC 350-20-35-22

The fair value of a reporting unit refers to the price that would be received to sell the unit as a whole in an orderly transaction between market participants at the measurement date. Quoted market prices in active markets are the best evidence of fair value and shall be used as the basis for the measurement, if available. However, the market price of an individual equity security (and thus the market capitalization of a reporting unit with publicly traded equity securities) may not be representative of the fair value of the reporting unit as a whole.

ASC 350-20-35-24

In estimating the fair value of a reporting unit, a valuation technique based on multiples of earnings or revenue or a similar performance measure may be used if that technique is consistent with the objective of measuring fair value. Use of multiples of earnings or revenue in determining the fair value of a reporting unit may be appropriate, for example, when the fair value of an entity that has comparable operations and economic characteristics is observable and the relevant multiples of the comparable entity are known. Conversely, use of multiples would not be appropriate in situations in which the operations or activities of an entity for which the multiples are known are not of a comparable nature, scope, or size as the reporting unit for which fair value is being estimated.

The FASB staff has noted that it would not be appropriate to use a valuation model based on the average of competitors' market values in determining a reporting unit's fair value. Additionally, the SEC staff has commented that entities should document the reasons why they use a valuation model based on factors other than market capitalization, including any reasons for deviating from market prices if that information is available. See further discussion in Section 3.3.4, "Control premiums."

Grant Thornton insight: Market capitalization and fair value of public entity with one reporting unit

When an entity has multiple reporting units, the fair value of each reporting unit should be individually determined. On the other hand, for public entities that have only one reporting unit, the entity's market capitalization (that is, the market price of one of the entity's public shares, multiplied by the number of shares outstanding) might approximate the entity's fair value and, therefore, be the fair value of the reporting unit.

However, the market capitalization of an entity inherently excludes the value of any control premium, which may be a material component when valuing the entity as a whole (see Section 3.3.4, "Control premiums"). As a result, an entity should consider whether it would expect a control premium to represent a significant component in determining its fair value before relying on its market capitalization as a basis for determining the fair value of the entity as a whole.

Income tax considerations on fair value

When determining the fair value of a reporting unit, an entity should consider whether the reporting unit could be bought or sold in a nontaxable, as opposed to a taxable, transaction. A reporting unit sold in a taxable transaction would generally result in a higher fair value and a lower impairment loss compared to a reporting unit sold in a nontaxable transaction. The guidance in ASC 350-20-35-25 through 35-27 notes that assuming a reporting unit could be bought or sold in a nontaxable or taxable transaction is a matter of judgment that depends on relevant facts and circumstances. Some considerations include whether market participants incorporate income taxes into their fair value estimates and whether the assumed structure is feasible and results in the highest and best economic use to the seller.

ASC 350-20-35-25 (Excerpt)

Before estimating the fair value of a reporting unit, an entity shall determine whether that estimation should be based on an assumption that the reporting unit could be bought or sold in a nontaxable transaction or a taxable transaction. Making that determination is a matter of judgment that depends on the relevant facts and circumstances and must be evaluated carefully on a case-by-case basis.

ASC 350-20-35-26

In making that determination, an entity shall consider all of the following:

a. Whether the assumption is consistent with those that marketplace participants would incorporate into their estimates of fair value

b. The feasibility of the assumed structure

c. Whether the assumed structure results in the highest and best use and would provide maximum value to the seller for the reporting unit, including consideration of related tax implications.

ASC 350-20-35-27

In determining the feasibility of a nontaxable transaction, an entity shall consider, among other factors, both of the following:

a. Whether the reporting unit could be sold in a nontaxable transaction

b. Whether there are any income tax laws and regulations or other corporate governance requirements that could limit an entity's ability to treat a sale of the unit as a nontaxable transaction.

3.3.3 Comparing the reporting unit carrying amount to fair value

When performing the quantitative goodwill impairment test, an entity compares a reporting unit's carrying amount to its fair value. If the carrying amount exceeds fair value, goodwill impairment equals the excess between those amounts, not to exceed the total amount of goodwill allocated to the reporting unit.

As part of the quantitative impairment test, an entity must also consider whether goodwill is tax deductible, as noted in ASC 350-20-35-8. If it is tax deductible, the calculation of a goodwill impairment loss may cause a change in deferred taxes that might impact the recognition of the goodwill impairment loss and require a specific calculation to determine the impairment loss, as discussed in "Quantitative impairment test when goodwill is tax deductible."

ASC 350-20-35-4

The quantitative goodwill impairment test, used to identify both the existence of impairment and the amount of impairment loss, compares the fair value of a reporting unit with its carrying amount, including goodwill.

ASC 350-20-35-6

If the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not impaired.

ASC 350-20-35-8

If the carrying amount of a reporting unit exceeds its fair value, an impairment loss shall be recognized in an amount equal to that excess, limited to the total amount of goodwill allocated to that reporting unit. Additionally, an entity shall consider the income tax effect from any tax deductible goodwill on the carrying amount of the reporting unit, if applicable, in accordance with paragraph 350-20-35-8B when measuring the goodwill impairment loss.

Quantitative impairment test when goodwill is not tax deductible

Goodwill is deductible for tax purposes for some business combination transactions. For example, goodwill created in an acquisition structured as an asset sale is deductible for tax purposes, while goodwill created in an acquisition structured as a stock sale is neither tax deductible nor amortizable for tax reporting purposes. For transactions that result in goodwill that is not tax deductible or that occur in jurisdictions where goodwill is not tax deductible, entities are not required to consider the deferred tax effects on any goodwill impairment loss recognized for a reporting unit.

The following example illustrates a goodwill impairment test when goodwill is not tax deductible.

Impairment test of a reporting unit for goodwill that is not tax deductible

APG Corp. has assessed goodwill from an acquisition of a reporting unit that is not tax deductible. The reporting unit has a carrying amount of goodwill of $1,000, other intangible assets of $500, other assets of $500, and liabilities of $500, resulting in a total carrying amount of $1,500. The fair value of the reporting unit is estimated as $900, as shown below.

	Carrying amount	Fair value	Impairment	Carrying amount after impairment
Goodwill	$1,000	$ -	$(600)	$400
Intangible assets	500	-	-	500
Assets	500		-	500
Liabilities	(500)	-	-	(500)
Net assets	$1,500	$900	$(600)	$900

In this example, a goodwill impairment charge of $600 (the carrying amount of $1,500 in net assets, minus the fair value of $900) is recognized for the reporting unit as a reduction of goodwill.

Quantitative impairment test when goodwill is tax deductible

Under the guidance in ASC 350-20-35-8, goodwill impairment is calculated as the amount by which the carrying amount of a reporting unit exceeds its fair value, limited to the total amount of goodwill of the reporting unit. When measuring a goodwill impairment loss, an entity must consider the impact of income tax effects of any tax-deductible goodwill on the carrying amount of the reporting unit. A decrease in the book value of goodwill resulting from an impairment charge will increase the deferred tax asset or decrease the tax liability while increasing the carrying amount of the reporting unit, causing the carrying amount to exceed its fair value immediately after recording the impairment charge and requiring *another* impairment charge (see ASC 350-20-35-8B). As a result, the guidance in ASC 350-20-35-8B allows entities to use a “simultaneous equation” for calculating the goodwill impairment charge and the deferred tax effects. Without the simultaneous equation, the impairment of the goodwill creates a cycle of impairment, because decreasing goodwill increases the deferred tax asset so that the carrying amount of the reporting unit increases without increasing its fair value.

ASC 350-20-35-8B

If a reporting unit has tax deductible goodwill, recognizing a goodwill impairment loss may cause a change in deferred taxes that results in the carrying amount of the reporting unit immediately exceeding its fair value upon recognition of the loss. In those circumstances, the entity shall calculate the impairment loss and associated deferred tax effect in a manner similar to that used in a business combination in accordance with the guidance in paragraphs 805-740-55-9 through 55-13. The total loss recognized shall not exceed the total amount of goodwill allocated to the reporting unit. See Example 2A in paragraphs 350-20-55-23A through 55-23C for an illustration of the calculation.

The following example illustrates the use of the simultaneous equation method for purposes of calculating impairment when the goodwill is tax deductible.

Impairment test using the simultaneous equation when goodwill is tax deductible

APG Corp. has goodwill that is tax deductible resulting from an acquisition that resulted in a new reporting unit. The reporting unit has a carrying amount of goodwill of $1,000, other intangible assets of $500, tangible assets of $100, and liabilities of $500, resulting in a total carrying amount of $1,100. The reporting unit is subject to a 25 percent income tax rate. The fair value of the reporting unit is estimated as $1,000, as shown in the following table.

	Carrying amount	Fair value	Preliminary impairment	Deferred tax asset adjustment	Carrying amount after impairment
Goodwill	$1,000	$ -	$(100)	$ -	$900
Intangible assets	500	-	-	-	500
Deferred tax asset	-	-	-	25	25
Tangible assets	100	-	-	-	100
Liabilities	(500)	-	-	-	(500)
Net assets	$1,100	$1,000	$(100)	$25	$1,025

The carrying amount of the reporting unit is $1,025 after adjusting the deferred tax asset to reflect the 25 percent tax-rate impact of the $100 goodwill impairment, which results in the carrying amount

($1,025) exceeding fair value ($1,000) by $25. APG Corp. then applies the simultaneous equation as follows:

Simultaneous equation: (tax rate ÷ [1 − tax rate]) x (impairment charge)

Deferred tax asset = (25% ÷ [1 − 25%]) x $100 = $33 (rounded)

	Carrying amount	Fair value	Preliminary impairment	Deferred tax asset adjustment	Carrying amount after impairment
Goodwill	$1,000	$ -	$(100)	$(33)	$867
Intangible assets	500	-	-	-	500
Deferred tax asset	-	-	-	33	33
Tangible assets	100	-	-	-	100
Liabilities	(500)	-	-	-	(500)
Net assets	$1,100	$1,000	$(100)	$ -	$1,000

APG Corp. recognizes a total of $133 as the goodwill impairment charge as well as an increase in deferred tax assets of $33. The total carrying amount of the reporting unit equals the fair value of the reporting unit after recognizing the goodwill impairment.

Grant Thornton insight: Tax considerations when goodwill impairment loss exceeds the reporting unit's goodwill

If the goodwill impairment loss exceeds the goodwill carrying amount after applying the simultaneous equation, an entity should follow the deferred tax asset guidance in ASC 740-10.

For example, say that an entity has $500 of goodwill for a reporting unit whose carrying amount exceeds its fair value by $450 and, accordingly, a goodwill impairment of $450 before applying the simultaneous equation. Applying the simultaneous equation increases the goodwill impairment by the amount of the deferred-tax impact adjustment at a 25% tax rate ($150), but the total goodwill impairment may not exceed the $500 pre-impairment carrying amount of the goodwill.

In this example, the $150 adjustment to the amount of goodwill impairment from applying the simultaneous equation ([25% tax rate ÷ (1 – 25%)] x $450 = $150) exceeds the goodwill balance of $500 by $100 ($450 impairment + $150 deferred tax impact = $600, which is greater than the pre-impairment carrying amount of goodwill of $500 by $100), and the deferred tax impact adjustment would be capped at the goodwill balance of $500, resulting in additional impairment of $50. However, the entity would still follow the guidance in ASC 740 on recognizing the deferred tax adjustment related to the impairment loss after applying the simultaneous equation, which is based on the difference between the goodwill amount on the entity's books—now zero—and the basis in the goodwill for tax purposes.

3.3.4 Control premiums

According to ASC 350-20-35-23, a "control premium" is the additional value or amount that an acquirer is willing to pay to obtain control of an entity and is derived from the ability to take advantage of synergies and other benefits as a result of controlling an entity's activities. This value is not reflected in an entity's market capitalization because market capitalization is expressed as the entity's share price multiplied by the number of outstanding shares. A control premium often occurs as a result of an acquiring entity being willing to pay more for equity securities that give it a controlling interest in an acquired entity than an investor would pay for a number of equity securities representing less than a controlling interest. According to the guidance in ASC 350-20-35-23, that substantial value may arise from the synergies that exist if an entity controls all of the operations of its reporting unit(s) that are operated together, thereby enhancing each reporting unit's cash flows because of cost efficiencies and additional revenue opportunities resulting from controlling all of the entity's reporting units. These synergies increase the value of the individual reporting units when valued separately, which could result in a premium in the total fair value of all reporting units exceeding the entity's market capitalization.

The SEC staff has noted that the difference between the entity's fair value and its market capitalization (that is, the control premium) should be reasonable, reconciled to market capitalization, and supported with market data, even though this assessment is not required by U.S. GAAP. The SEC staff may request that a registrant provide evidence to support a control premium. The level of evidence and documentation required to support the control premium increases as the control premium increases. If an entity cannot support the reasonableness of the control premium with market data, it may need to reassess the fair value of its individual reporting units and the reasonableness of the individual fair value assumptions used to arrive at a reasonable and supportable control premium. If the reporting units' fair values are revised, the entity may also need to reassess its goodwill impairment test for each reporting unit.

An entity should analyze the facts and circumstances of its situation when determining whether a control premium exists. In making this determination, an entity should consider trends in market capitalization over a reasonable period of time but should not ignore a recent decline in stock price. There is no "rule of thumb" guidance defining "a reasonable period of time," so this evaluation may require employing significant judgment.

Grant Thornton insight: SEC staff focuses on control premiums

At the 2008 AICPA Conference on Current SEC and PCAOB Developments, the SEC staff noted that an entity's market capitalization may not equal the combined fair value of all of its individual reporting units together. Control premium is expressed as the excess of the total fair value of an entity's reporting units over the entity's market capitalization. However, the SEC staff noted at the 2008 conference that determining a reasonable and acceptable amount of control premium in excess of market capitalization may require a great deal of judgment, since there are no "bright line" tests to determine the reasonableness of a control premium. Instead, an entity must carefully analyze the particular facts and circumstances of its situation when determining an appropriate control premium. A control premium percentage over an entity's market cap that is arbitrary or allows an entity to avoid impairment would not be considered appropriate.

If a public entity concludes that its current market capitalization does not reflect the entity's fair value, it must have appropriate support from the marketplace indicating why the level of control premium is appropriate. At the 2008 SEC conference, the staff noted that it is prudent to reconcile the combined fair value of an entity's reporting units to its market capitalization, although the reconciliation should not be viewed as the only factor to consider when assessing goodwill for impairment. An entity should assess its valuations and corresponding assumptions if there is a large implied control premium that cannot be supported with other market evidence. "Acceptable support" for a control premium may include evaluation of control premiums identified in comparable transactions or the cash flows associated with obtaining control of a reporting unit. An entity must carefully evaluate its particular facts and circumstances, and use reasonable judgment, when determining an appropriate control premium. An implied control premium that cannot be supported by market evidence or is deemed to be unreasonable may require a reevaluation of the fair values of the individual reporting units and the assumptions used to value those units.

Public entities should also consider recent trends in their market capitalization. In volatile markets, it may be appropriate to look at market capitalization over a reasonable period of time leading up to the impairment testing date, as opposed to using a single day's market capitalization. What constitutes a "reasonable" period of time, however, is a matter of judgment, and an entity should consider recent relevant events and trends in its share price when determining a reasonable period. Entities need to support the range of dates used to determine market capitalization and should not ignore a recent decline in share price.

The following example shows considerations when supporting a control premium.

Control premium

APG Inc. has five reporting units. At the date of its annual goodwill impairment test, APG Inc. determines the fair value of all five of its reporting units totals $150 million. The share price at the entity's annual goodwill impairment testing date is $60 per share, with 2 million shares outstanding. The calculation of the implied control premium is shown below:

(a) Total fair value of the five reporting units = $150 million

(b) Market capitalization = $120 million ($60 per share at 2 million shares)

(c) Implied control premium = $30 million [(a) – (b)]

In this example, APG has a 25 percent control premium ($30 million control premium ÷ $120 million market capitalization) that is supported by additional market evidence, such as control premiums in comparable transactions, which indicates that the control premium is reasonable and not excessive.

Determining a "reasonable" implied control premium may be challenging and might require the use of a valuation expert. In September 2017, the Appraisal Foundation issued Valuation in Financial Reporting Valuation Advisory 3, *The Measurement and Application of Market Participant Acquisition Premiums*, which provides best practices to use when determining the reasonableness of an implied control premium.

If APG cannot support the control premium with market data, it would need to reassess the valuations and corresponding assumptions for each individual reporting unit valuation and adjust these valuations and assumptions to support a lower, more reasonable control premium evidenced by market data. This reassessment might cause additional goodwill impairment for the reporting units as a result of these adjustments to the units' fair values.

3.3.5 Subsequent event considerations when market capitalization declines

An entity should carefully consider whether a decline in share price and, accordingly, in market capitalization that occurs after the reporting period, but before the financial statements are issued, denotes an existing condition at the reporting date that might be an indicator of impairment at period-end, which should be considered in any goodwill impairment testing. Said differently, an entity should consider facts and circumstances to determine why the decline is *not* related to conditions that existed at period-end, but instead relates to conditions that occurred after the period-end reporting date.

3.3.6 Subsidiary level goodwill impairment testing for stand-alone subsidiary reporting

If an entity has a subsidiary that issues stand-alone financial statements, the goodwill impairment test for the stand-alone subsidiary's financial statements is performed at the level of the subsidiary's reporting unit(s), as described in ASC 350-20-35-47 through 35-48. In other words, the subsidiary tests goodwill for impairment as though the subsidiary were a stand-alone entity—that is, reporting units for purposes of testing goodwill for impairment, as well as the goodwill impairment that is recognized, are determined based on the subsidiary as a stand-alone entity.

An impairment loss that exists at the subsidiary level when reporting on the subsidiary's stand-alone financial statements may be different from an impairment loss recognized by the subsidiary's parent. In other words, a goodwill impairment loss recognized in a subsidiary's stand-alone financial statements does not automatically translate to an impairment loss for the subsidiary's parent. Instead, the parent entity should consider whether the subsidiary's goodwill impairment indicates that goodwill impairment might also exist at the consolidated level and that the goodwill of the parent's reporting unit including the subsidiary should be tested when preparing the parent entity's financial statements. Said another way, if a goodwill impairment loss is recognized at the subsidiary level, goodwill of the reporting unit or units (at the higher consolidated level) in which the subsidiary's reporting unit with impaired goodwill resides must be tested for impairment if the event that gave rise to the loss at the subsidiary level would more likely than not reduce the fair value of the reporting unit at the higher consolidated level below its carrying amount. Similarly, if goodwill impairment exists at the level of the parent entity's consolidated financial statements, that impairment should not be automatically pushed down to the subsidiary's stand-alone financial statements. It is generally unlikely that the amount of impairment, if any, recognized by the parent entity will be same as the impairment recognized in the stand-alone financial statements of a subsidiary.

ASC 350-20-35-47

Subsidiary goodwill might arise from any of the following:

a. Acquisitions that a subsidiary made prior to its being acquired by the parent

b. Acquisitions that a subsidiary made subsequent to its being acquired by the parent

c. Goodwill arising from the business combination in which a subsidiary was acquired that the parent pushed down to the subsidiary's financial statements.

ASC 350-20-35-48

All goodwill recognized by a public or nonpublic subsidiary (subsidiary goodwill) in its separate financial statements that are prepared in accordance with generally accepted accounting principles (GAAP) shall be accounted for in accordance with this Subtopic. Subsidiary goodwill shall be tested for impairment at the subsidiary level using the subsidiary's reporting units. If a goodwill impairment loss is recognized at the subsidiary level, goodwill of the reporting unit or units (at the higher consolidated level) in which the subsidiary's reporting unit with impaired goodwill resides must be tested for impairment if the event that gave rise to the loss at the subsidiary level would more likely than not reduce the fair value of the reporting unit (at the higher consolidated level) below its carrying amount (see paragraph 350-20-35-3C(f)). Only if goodwill of that higher-level reporting unit is impaired would a goodwill impairment loss be recognized at the consolidated level.

ASC 350-20-35-49

If testing at the consolidated level leads to an impairment loss, that loss shall be recognized at that level separately from the subsidiary's loss.

4 Private Company Council goodwill accounting alternatives

The FASB's Private Company Council (PCC), in an effort to reduce the cost and complexity of accounting for goodwill, developed a series of accounting alternatives that are available to private entities:

- The accounting alternative for amortizing goodwill introduced by ASU 2014-02, which is codified in ASC 350-20-35-62 through 35-64;
- The accounting alternative for evaluating triggering events only at the end of a reporting period introduced by ASU 2021-03, codified in ASC 350-20-35-84 through 35-85; and
- The accounting alternative to forego separately recognizing certain intangible assets from goodwill in a business combination introduced by ASU 2014-18, codified in ASC 805-20-25-29 through 25-33

The alternatives were developed as a result of stakeholders' feedback indicating that the cost and complexity of accounting for goodwill exceeded the benefits. Stakeholders reasoned that some users of private entity financial statements disregard goodwill and any related impairment, as they often adjust U.S. GAAP amounts for assets and income or losses by removing goodwill and impairment charges from those amounts when using a private entity's financial information. In addition, while the optional qualitative assessment for goodwill impairment testing provided some simplification and cost savings for private entities, these savings were generally not significant.

When elected by private entities, the PCC alternatives are designed to reduce the complexity associated with the accounting for goodwill by

a. Allowing private entities to amortize goodwill;

b. Simplifying the goodwill impairment testing, including how to determine the level or unit of account at which to test;

c. Allowing private entities to determine whether a triggering event has occurred by evaluating facts and circumstances only at a financial reporting date as opposed to during the reporting period; and

d. Permitting private entities to subsume certain customer-related and noncompetition-related intangibles into goodwill.

Because the goodwill accounting alternatives are available only to private entities, determining whether an entity meets the definition of a "private company," as defined in the Master Glossary to the FASB's Codification, is the first step in assessing an entity's eligibility.

Private Company

An entity other than a public business entity, a not-for-profit entity, or an employee benefit plan within the scope of Topics 960 through 965 on plan accounting.

An entity should carefully consider whether it meets the private company definition before electing to apply the goodwill alternatives, which means that the entity must *not* meet the criteria of a public business entity. In other words, an entity meeting the definition of a private company would not meet any of the criteria in the Master Glossary definition of a public business entity, as shown below.

Public Business Entity

A public business entity is a business entity meeting any one of the criteria below. Neither a not-for-profit entity nor an employee benefit plan is a business entity.

a. It is required by the U.S. Securities and Exchange Commission (SEC) to file or furnish financial statements, or does file or furnish financial statements (including voluntary filers), with the SEC (including other entities whose financial statements or financial information are required to be or are included in a filing).

b. It is required by the Securities Exchange Act of 1934 (the Act), as amended, or rules or regulations promulgated under the Act, to file or furnish financial statements with a regulatory agency other than the SEC.

c. It is required to file or furnish financial statements with a foreign or domestic regulatory agency in preparation for the sale of or for purposes of issuing securities that are not subject to contractual restrictions on transfer.

d. It has issued, or is a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market.

e. It has one or more securities that are not subject to contractual restrictions on transfer, and it is required by law, contract, or regulation to prepare U.S. GAAP financial statements (including notes) and make them publicly available on a periodic basis (for example, interim or annual periods). An entity must meet both of these conditions to meet this criterion.

An entity may meet the definition of a public business entity solely because its financial statements or financial information is included in another entity's filing with the SEC. In that case, the entity is only a public business entity for purposes of financial statements that are filed or furnished with the SEC.

In applying the definitions of *private company* and *public business entity*, an entity may be considered a public business entity solely because its financial information or financial statements are included in another entity's filing with the SEC. In that situation, an entity is considered to be a public business entity only for the purposes of including its financial information in another entity's financial statements that are filed with the SEC. In this situation, the entity is not considered to be a public business entity for purposes of its stand-alone financial statements, which are not filed or furnished with the SEC. As a result, it would be permitted to elect the PCC accounting alternative for goodwill for those stand-alone financial statements.

Grant Thornton insight: Choosing to apply private company alternatives

A private entity should consider its future plans and stakeholders' requirements and expectations, among other factors, before electing to apply a private company accounting alternative. For instance, it is important to consider whether the owner's exit strategy includes an IPO. In this scenario, the entity's financial statements would need to be retroactively restated—to remove the effects of electing the alternatives as a private entity—to comply with SEC rules. Similarly, if a potential exit strategy is a sale to a public business entity, then the entity might decide that the costs to reverse a private company accounting alternative do not outweigh the benefits.

For example, if an entity is required to report as a public business entity due to an IPO or a sale to a public company after it has already elected a private company accounting alternative, the entity would then be required to retrospectively reconstruct its goodwill accounting to apply the public entity accounting and reporting requirements to all periods presented. This task could be challenging and time-intensive, as it would require accounting and valuation considerations of information that was known or knowable in each previous reporting period that has elapsed since the private company alternative was elected.

Prior to deciding whether to adopt any private company alternative, an entity should also ensure that its stakeholders, including investors, lenders, and others, will agree to accept financial statements that reflect its application. We believe that some stakeholders might expect an entity to prepare financial statements that can be used for either public entity or private company purposes, and would find adopting the alternatives unacceptable. Therefore, entities should have thorough discussions of the potential impact of adoption with those parties and address the specific needs of each stakeholder when making a decision.

A private entity should also consider whether its investors include a public business entity holding an equity method investment. If so, any benefit from electing private company accounting alternatives would likely be offset by the cost of complying with public business entity requirements for purposes of the equity method investor's accounting for its investment.

Adoption of private company accounting alternatives

The adoption of a private company accounting alternative is optional. A private company that has not yet adopted an accounting alternative may initially adopt an alternative after it is initially eligible for adoption, without justifying that the use of the accounting alternative is preferable. Any subsequent change to that accounting policy election requires justification that the change is preferable under the guidance in ASC 250. The guidance for adopting the accounting alternatives is included below.

ASC 350-20-65-2

The following represents the transition information related to Accounting Standards Updates No. 2014-02, *Intangibles—Goodwill and Other (Topic 350): Accounting for Goodwill*, No. 2019-06, *Intangibles—Goodwill and Other (Topic 350), Business Combinations (Topic 805), and Not-for-Profit Entities (Topic 958): Extending the Private Company Accounting Alternatives on Goodwill and Certain Identifiable Intangible Assets to Not-for-Profit Entities*, and No. 2021-03, *Intangibles—Goodwill and Other (Topic 350): Accounting Alternative for Evaluating Triggering Events* referenced in paragraph 350-20-15-3A:

a. Upon adoption of the guidance for the accounting alternative for amortizing goodwill in the Accounting Alternatives Subsections of this Subtopic and the guidance in paragraph 323-10-35-13, that guidance shall be effective prospectively for new goodwill recognized after the adoption of that guidance. For existing goodwill, that guidance shall be effective as of the beginning of the first fiscal year in which the accounting alternative is adopted.

b. Goodwill existing as of the beginning of the period of adoption shall be amortized prospectively on a straight-line basis over 10 years, or less than 10 years if an entity demonstrates that another useful life is more appropriate.

c. [Subparagraph superseded by Accounting Standards Update No. 2016-03].

d. Upon adoption of the accounting alternative for amortizing goodwill, an entity shall make an accounting policy election to test goodwill for impairment at either the entity level or the reporting unit level.

e. A private company or not-for-profit entity that makes an accounting policy election to apply the accounting alternative for amortizing goodwill in the Accounting Alternatives Subsections of this Subtopic for the first time need not justify that the use of the accounting alternative is preferable as described in paragraph 250-10-45-2.

ASC 350-20-65-3

The following represents the transition and effective date information related to Accounting Standards Updates No. 2017-04, *Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment,* No. 2019-10, *Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842): Effective Dates*, and No. 2021-03, *Intangibles—Goodwill and Other (Topic 350): Accounting Alternative for Evaluating Triggering Events*:

ASC 350-20-65-3e

Private companies that have adopted the private company accounting alternative for amortizing goodwill or the private company accounting alternative for a goodwill impairment triggering event evaluation but have not adopted the private company alternative for subsuming certain intangible assets into goodwill are allowed, but not required, to adopt this guidance prospectively on or before the effective date without having to justify preferability of the accounting change. Private companies that have adopted the private company alternative to subsume certain intangible assets into goodwill and, thus, also adopted the goodwill alternative are not permitted to adopt this guidance upon issuance without following the guidance in Topic 250 on accounting changes and error corrections, including justifying why it is preferable to change their accounting policies.

ASC 350-20-65-4

The following represents the transition and effective date information related to Accounting Standards Update No. 2021-03, *Intangibles—Goodwill and Other (Topic 350): Accounting Alternative for Evaluating Triggering Events:*

a. The pending content that links to this paragraph shall be effective prospectively for fiscal years beginning after December 15, 2019. Early adoption is permitted for both interim and annual financial statements that have not yet been issued or made available for issuance as of March 30, 2021. A private company or not-for-profit entity that adopts the pending content that links to this paragraph shall apply it as of the beginning of the interim or annual period for financial statements that have not yet been issued or made available for issuance in the year of adoption. A private company or not-for-profit entity shall not retroactively adopt the pending content that links to this paragraph as of the beginning of an annual period for which interim-period financial statements have already been issued in the year of adoption.

b. For a private company or not-for-profit entity that adopts the pending content that links to this paragraph after its original effective date, that pending content shall be applied prospectively as of the beginning of the first reporting period in which the accounting alternative is adopted.

c. A private company or not-for-profit entity that makes an accounting policy election to apply the pending content that links to this paragraph for the first time need not justify that the use of the accounting alternative is preferable as described in paragraph 250-10-45-2.

ASC 805-20-65-2

The following represents the transition information related to Accounting Standards Updates No. 2014-18, *Business Combinations (Topic 805): Accounting for Identifiable Intangible Assets in a Business Combination,* and No. 2019-06, *Intangibles—Goodwill and Other (Topic 350), Business Combinations (Topic 805), and Not-for-Profit Entities (Topic 958): Extending the Private Company Accounting Alternatives on Goodwill and Certain Identifiable Intangible Assets to Not-for-Profit Entities,* referenced in paragraph 805-20-15-1A:

a. Upon adoption of the Accounting Alternative Subsections of this Subtopic, that guidance shall be effective prospectively to the first transaction that is identified in paragraph 805-20-15-2 after the adoption of the accounting alternative.

b. Customer-related intangible assets and noncompetition agreements that exist as of the beginning of the period of adoption shall continue to be subsequently measured in accordance with Topic 350 on intangibles—goodwill and other. That is, existing customer-related intangible assets and noncompetition agreements should not be subsumed into goodwill upon adoption of the Accounting Alternative Subsections of this Subtopic.

c. [Subparagraph superseded by Accounting Standards Update No. 2016-03].

d. A private company or not-for-profit entity that makes an accounting policy election to apply the guidance in the Accounting Alternative Subsections of this Subtopic for the first time need not justify that the use of the accounting alternative is preferable as described in paragraph 250-10-45-2.

4.1 Amortization of goodwill accounting alternative

A private entity or a not-for-profit (NFP) entity (that is, an entity other than a public business entity) has the option to elect the accounting alternative to amortize goodwill in accordance with ASC 350-20-35-62 through 35-64. Under this alternative, a private entity or NFP may elect to amortize goodwill on a straight-line basis over 10 years or a shorter time period if the entity demonstrates that another useful life is more appropriate. Once elected, the goodwill amortization accounting alternative must be applied to all existing goodwill and any future goodwill acquired through future transactions.

Goodwill that exists when a private entity elects to adopt the accounting alternative to amortize goodwill should be amortized prospectively on a straight-line basis over 10 years, even if the goodwill was previously recognized. The goodwill that exists at the time of adoption may be amortized over a period that is less than 10 years if an entity demonstrates that another useful life is more appropriate, as discussed in Section 4.1.1, "Determining the amortization period." The individual amortizable units of goodwill (that is, the unit of account used for amortizing goodwill) is based on each individual business combination, acquisition, or application of fresh-start accounting. Each individual acquisition that results in an addition to goodwill represents a separate amortizable unit of goodwill that will be assigned a separate useful life.

ASC 350-20-35-62

The following guidance for goodwill applies to entities within the scope of paragraph 350-20-15-4 that elect the accounting alternative for amortizing goodwill.

ASC 350-20-35-63

Goodwill relating to each business combination, acquisition by a not-for-profit entity, or reorganization event resulting in fresh-start reporting (amortizable unit of goodwill) shall be amortized on a straight-line basis over 10 years, or less than 10 years if the entity demonstrates that another useful life is more appropriate.

ASC 350-20-35-64

An entity may revise the remaining useful life of goodwill upon the occurrence of events and changes in circumstances that warrant a revision to the remaining period of amortization. However, the cumulative amortization period for any amortizable unit of goodwill cannot exceed 10 years. If the estimate of the remaining useful life of goodwill is revised, the remaining carrying amount of goodwill shall be amortized prospectively on a straight-line basis over that revised remaining useful life.

Grant Thornton insight: Amortizing goodwill with multiple business combinations

When a private entity or NFP enters into multiple business combinations over a period of time or applies “fresh-start accounting,” as described in ASC 852, the goodwill associated with each business combination or application of fresh-start accounting (that is, each “unit of goodwill”) should be tracked and amortized separately over 10 years (unless a shorter period is demonstrated to be more appropriate) from each goodwill initial recognition event. “Fresh-start accounting” allows an entity emerging from bankruptcy to present its assets, liabilities, and equity as a new entity on a current fair-value basis if certain criteria are met.

However, for purposes of testing goodwill for impairment, goodwill generated from each business combination or application of fresh-start accounting should be aggregated by reporting unit or for the entity as a whole if the goodwill impairment testing alternative is elected, as discussed in Section 4.2, “Simplification of level and frequency of testing.”

4.1.1 Determining the amortization period

A private entity or NFP that elects to use the accounting alternative to amortize goodwill should amortize goodwill on a straight-line basis over 10 years, unless the entity can demonstrate that a period less than 10 years is more appropriate. A useful life greater than 10 years may not be used under the guidance in ASC 350-20-35-63 to 35-64. Useful life determinations require significant judgment based on the particular facts and circumstances in each case. For example, an amortization period of less than 10 years could be more appropriate if an acquiree has key technology or other intellectual property that has a lifespan of less than 10 years and that asset is the key driver of the acquiree’s value. In this situation, an amortization period of less than 10 years for the goodwill might be more appropriate.

Goodwill amortized over a useful life shorter than 10 years

Entity A acquires a company with a technology license that has a remaining life of eight years, which is the key driver of the acquiree's value. Entity A then demonstrates that an eight-year amortization period for the goodwill recognized from this acquisition is more appropriate than ten years because the technology can only be used for eight years after the acquisition and is a key driver in goodwill value.

The useful life of a unit of goodwill may be revised based on changes in events and circumstances, but the cumulative amortization period cannot exceed 10 years for each unit of goodwill. If the remaining useful life is revised, the change should be treated as a change in accounting estimate under ASC 250, and the carrying amount of goodwill at that time should be prospectively amortized on a straight-line basis over the remaining term of the revised period.

Revised goodwill amortization period

Assume the same facts as in the previous example. After two years of amortizing the technology license, however, Entity A becomes aware of a competitor's new licensed product that will render Entity A's technology obsolete in two additional years, resulting in a change in the remaining life of the technology asset. As a result, Entity A amortizes the unamortized portion of the technology prospectively over the new two-year (rather than six-year) remaining life of the asset. As a result of the change in the life of the technology license the goodwill amortization period must also be reassessed as the technology license was the key driver of the original acquiree's value and accordingly the key driver for the life of the goodwill. The entity changes the remaining life of the entity's goodwill and amortizes the unamortized portion of the goodwill prospectively over the new two-year (rather than six-year) remaining life of the goodwill. There is no adjustment to previously amortized goodwill, as stipulated under ASC 350-20-35-64.

4.1.2 Recognition of an impairment loss

If a private entity or NFP using the accounting alternative to amortize goodwill identifies a goodwill impairment loss after considering the impairment triggering events discussed in Section 3.2.4, "Interim impairment considerations" (and the accounting alternatives for private entities and NFPs discussed in Section 4.2, "Simplification of level and frequency of impairment testing") and after performing a quantitative goodwill impairment test as discussed in Section 3.3, "Performing the quantitative goodwill impairment test," the loss should be allocated to the individual amortizable units of goodwill on a pro rata basis, using their relative carrying amounts (or another reasonable or rational basis). An "amortizable" unit of goodwill is the unit of account used for amortizing goodwill based on each prior business combination, acquisition, or application of fresh-start accounting, as discussed in Section 4.1, "Amortization of goodwill accounting alternative."

Unless impairment testing is performed at the amortizable unit of goodwill level, entities will be required to allocate any impairment loss. Impairment losses are always allocated to amortizable units of goodwill, so if there is more than one amortizable unit of goodwill and if impairment testing is conducted at a different level, entities will need to allocate the impairment loss. For example, a nonpublic entity that elects to test goodwill for impairment at the entity level, as discussed in

Section 4.2, “Simplification of level and frequency of impairment testing,” should allocate impairment losses to the entity’s amortizable units of goodwill. Nonpublic entities that test goodwill for impairment at the reporting unit level should allocate impairment losses to those amortizable units of goodwill of the impaired reporting unit.

After a goodwill impairment loss is recognized, the adjusted carrying amount of the amortizable units of goodwill becomes the new accounting basis for the goodwill. The new basis of accounting is then amortized over the remaining useful life of the goodwill unit. The subsequent reversal of any previously recognized goodwill impairment loss is prohibited under ASC 350-20-35-78.

ASC 350-20-35-77

The goodwill impairment loss, if any, shall be allocated to individual amortizable units of goodwill of the entity (or the reporting unit) on a pro rata basis using their relative carrying amounts or using another reasonable and rational basis.

ASC 350-20-35-78

After a goodwill impairment loss is recognized, the adjusted carrying amount of goodwill shall be its new accounting basis, which shall be amortized over the remaining useful life of goodwill. Subsequent reversal of a previously recognized goodwill impairment loss is prohibited.

Impairment loss allocation for entities with multiple amortizable units of goodwill

Entity A, a private entity that has previously adopted the PCC accounting alternative to amortize goodwill under ASC 350-20, has also elected to test goodwill for impairment at the overall entity level as opposed to the reporting unit level. Upon adoption of the private company alternative, Entity A assigns a 10-year useful life to its one existing amortizable unit of goodwill.

Since the adoption, Entity A completes two business combinations, each resulting in additional amortizable units of goodwill, which are being amortized separately over a 10-year period starting from the respective acquisition dates. As a result, Entity A now has a total of three amortizable units of goodwill.

On July 1 of the current year, Entity A identifies a triggering event—that is, circumstances that indicate it is more likely than not that the fair value of the reporting unit (which is the entity as a whole) is less than its carrying value. The carrying value of goodwill as of the triggering event date is determined by recognizing applicable amortization through the date of the impairment triggering event, which in this case is July 1, 20X1.

Entity A elects to bypass the qualitative impairment assessment and proceeds directly to a quantitative impairment test. On July 1, 20X1, the carrying value of goodwill is $500,000, and the entity determines that the fair value of goodwill is $400,000, resulting in an impairment charge of $100,000.

Entity A allocates the $100,000 impairment loss to each amortizable unit of goodwill on a pro rata basis based on the relative carrying amount of each amortizable unit of goodwill, which is determined as shown in the following table.

As of July 1, 20X1	Unit 1	Unit 2	Unit 3	Total
Carrying value of goodwill	$ 200,000	$ 200,000	$ 100,000	$500,000
% of total carrying value	40%	40%	20%	
Allocated impairment loss	$ 40,000	$ 40,000	$20,000	$100,000

Once the appropriate loss allocation is calculated, Entity A allocates the impairment loss to each amortizable unit of goodwill as follows.

	Unit 1	Unit 2	Unit 3	Total
Carrying value of goodwill	$ 200,000	$ 200,000	$ 100,000	$ 500,000
Allocated impairment loss	(40,000)	(40,000)	(20,000)	(100,000)
Post-impairment carrying value of goodwill	$ 160,000	$ 160,000	$ 80,000	$ 400,000

Going forward, Entity A will continue to amortize the post-impairment carrying value of each amortizable unit of goodwill over the respective remaining useful life of each amortizable unit of goodwill.

4.1.3 Allocating goodwill to disposed businesses

When a nonpublic entity that amortizes goodwill disposes of a portion of a reporting unit, it must include goodwill in the disposed business’s carrying amount in order to determine the gain or loss on disposal. Under ASC 350-20-40-9, nonpublic entities that elect the goodwill amortization accounting alternative should include goodwill resulting from the disposal of a business that is part of a reporting unit in the disposed business’s carrying amount in order to determine the gain or loss on disposal. An entity should use a reasonable and rational approach to determine the amount of goodwill associated with the disposed business. Although the FASB considers a relative fair value approach for allocating goodwill to be reasonable (as discussed in Section 3.2.3, “Other circumstances requiring impairment testing,” and in ASC 350-20-40-3), other methods could be used that might be considered reasonable and rational for a nonpublic entity.

ASC 350-20-40-8

The following guidance for goodwill applies to entities within the scope of paragraph 350-20-15-4 that elect the accounting alternative for amortizing goodwill.

ASC 350-20-40-9

When a portion of an entity (or a reporting unit) that constitutes a business or nonprofit activity is to be disposed of, goodwill associated with that business or nonprofit activity shall be included in the carrying amount of the business or nonprofit activity in determining the gain or loss on disposal. An entity shall use a reasonable and rational approach to determine the amount of goodwill associated with the business or nonprofit activity to be disposed of.

Grant Thornton insight: Allocating goodwill to disposed businesses

The concept of allocating goodwill to a disposed business under the private company accounting alternative is similar to the longstanding requirement to include an allocation of goodwill in the carrying amount of a portion of a reporting unit disposed of under ASC 350-20-40-1 through 40-4. The accounting alternative does not specify how to determine that allocation, however, but simply indicates that it should be "reasonable and rational." For example, a nonpublic entity may use other methods, such as allocating goodwill based on a relative carrying amount basis, which might be considered reasonable and rational for a nonpublic entity.

This guidance contrasts with the requirement in ASC 350-20-40-3 to allocate goodwill based on the relative fair values of the disposed portion and the remaining portion of the reporting unit. Accordingly, nonpublic entities should have accounting policies in place surrounding disposals, and these policies should be applied consistently to all disposals. The accounting policy for allocating goodwill to disposed businesses could include a relative fair value approach, among other reasonable and rational approaches.

The following table compares the effect of applying the private company accounting alternative for amortizing goodwill versus applying the guidance in ASC 350-20-35-1.

Comparison of guidance with and without goodwill amortization alternative

Main provisions	Requirements without accounting alternative	Effect of accounting alternative*
Amortization	Not allowed	10 years straight line, or shorter if demonstrated as most appropriate
Allocating goodwill impairment to amortizable units	Not applicable	Allocated to amortizable goodwill units (at entity level or reporting unit level, depending at which level goodwill is tested) on a pro rata basis by carrying amount, or other reasonable and rational basis
Derecognition: disposal of a business	Relative fair values of business disposed to remaining reporting unit	Reasonable and rational allocation of goodwill to disposed business, with no required method of allocation

*Changes between accounting policies should be preferable in accordance with the guidance in ASC 250. In general, the alternative accounting policies would be less preferrable and, once adopted, would be difficult to “re-adopt” if an entity were to reverse its election of any accounting alternatives.

4.2 Simplification of level and frequency of impairment testing

Private entities that elect to adopt the accounting alternative to amortize goodwill may further simplify their accounting by electing to test goodwill for impairment at the overall entity level as opposed to testing at the reporting unit level.

Further, a nonpublic entity electing the goodwill amortization accounting alternative is required to perform a goodwill impairment test only when it identifies a triggering event (see Section 3.2.4, “Interim impairment considerations”), without a requirement to perform an annual impairment test. For nonpublic entities that elect the accounting alternative in ASC 350-20-35-84, a goodwill triggering event evaluation should be performed only at the end of each reporting period, as discussed in Section 4.3, “Accounting alternative for evaluating trigger events.”

Once a triggering event is identified, the entity may choose whether to perform a qualitative assessment under ASC 350-20-35-3A through 35-3G to determine whether it is more likely than not that the fair value of the reporting unit is less than its carrying amount or skip the qualitative assessment and proceed to a quantitative calculation of impairment under ASC 350-20-35-4 through 35-13 (see Section 3.2.2, “Optional qualitative goodwill assessment,” and Section 3.3, “Performing the quantitative goodwill impairment test,” respectively). This choice is made each time a triggering event occurs, and an entity may change its approach for each event (that is, it may choose to start with a qualitative assessment or go directly to a quantitative evaluation). As under the general guidance, an entity that elects this accounting alternative has the unconditional option to proceed directly to a quantitative impairment test rather than perform a qualitative assessment.

ASC 350-20-35-65

Upon adoption of this accounting alternative, an entity shall make an accounting policy election to test goodwill for impairment at the entity level or the reporting unit level. An entity that elects to perform its impairment tests at the reporting unit level shall refer to paragraphs 350-20-35-33 through 35-38 and paragraphs 350-20-55-1 through 55-9 to determine the reporting units of an entity.

ASC 350-20-35-66

Goodwill of an entity (or a reporting unit) shall be tested for impairment if an event occurs or circumstances change that indicate that the fair value of the entity (or the reporting unit) may be below its carrying amount (a triggering event). Paragraph 350-20-35-3C(a) through (g) includes examples of those events or circumstances. Those examples are not all-inclusive, and an entity shall consider other relevant events and circumstances that affect the fair value or carrying amount of the entity (or of a reporting unit) in determining whether to perform the goodwill impairment test. For those entities that have elected the accounting alternative for a goodwill impairment triggering event evaluation in paragraph 350-20-35-84, a goodwill triggering event evaluation shall be performed only as of the end of each reporting period. If an entity determines that there are no triggering events, then further testing is unnecessary.

ASC 350-20-35-67

Upon the occurrence of a triggering event, an entity may assess qualitative factors to determine whether it is more likely than not (that is, a likelihood of more than 50 percent) that the fair value of the entity (or the reporting unit) is less than its carrying amount, including goodwill. Paragraph 350-20-35-3C(a) through (g) includes examples of those qualitative factors.

ASC 350-20-35-68

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

ASC 350-20-35-69

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 the entity (or the 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 quantitative 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 quantitative goodwill impairment test.

ASC 350-20-35-70

An entity has an unconditional option to bypass the qualitative assessment described in paragraphs 350-20-35-67 through 35-69 and proceed directly to a quantitative calculation by comparing the entity's (or the reporting unit's) fair value with its carrying amount (see paragraphs 350-20-35-72 through 35-78). An entity may resume performing the qualitative assessment upon the occurrence of any subsequent triggering events.

Grant Thornton insight: Accounting alternative qualitative impairment assessment considerations

For a number of entities, especially those electing to test goodwill at the entity level, performing a qualitative assessment may not provide a cost or efficiency benefit compared with performing a quantitative calculation. In part, this is because many private entities periodically perform fair value calculations of the entity for purposes of stock compensation, stakeholder requirements, issuances of securities, and other reasons. Further, the effort involved in making a qualitative assessment requires an entity to gather and document considerable information related to marketplace and business environment factors as well as rates and assumptions used by market participants, among other information. As a result, an entity might determine that proceeding directly to a quantitative calculation could be more efficient.

The following table compares the accounting for entities either using or not using the goodwill impairment level and frequency of goodwill impairment testing simplifications under the private company alternative to amortize goodwill, as indicated in ASC 350-20-35-65 to 35-75.

Comparison of guidance with and without goodwill testing level and frequency alternatives under amortization alternative		
Main provisions	**Requirements without accounting alternative**	**Effects of accounting alternative***
Unit of account at which goodwill impairment is assessed	Reporting unit	Must elect at entity level or reporting unit level; this election is made when the accounting alternative is elected Subsequent change from entity level to reporting unit level, or vice versa, would be an ASC 250 accounting policy change and would need to be preferable
Annual impairment test	Required	No annual test; test only upon occurrence of triggering event
Sequencing of impairment tests	Other assets or asset groups are tested before goodwill	No change

* Changes between accounting policies should be preferable in accordance with the guidance in ASC 250. In general, the alternative accounting policies would be less preferrable and, once adopted, would be difficult to "re-adopt" if an entity were to reverse its election of any accounting alternatives.

Grant Thornton insight: Considerations when electing accounting alternatives

Private entities should carefully consider their future plans and intentions when determining whether to elect the accounting alternative to amortize goodwill as well as a policy for testing goodwill impairment. If the private entity has intentions of going public or if a potential exit strategy is a sale to a public business entity, then electing the private entity goodwill accounting alternative might make the transition from reporting using the PCC alternative to public entity reporting more difficult, as the entity will be required to reverse, or essentially "unwind," the private company accounting from the time when it elected the alternative to when it begins to report as a public business entity. This would include reversing the amortization and considering any changes in impairment testing that would have occurred had the accounting alternative not been elected. The longer the time period that elapses between the adoption of the accounting alternative (or the acquisition and recognition of goodwill) and the change from PCC reporting to reporting as a public business entity, the more time and effort will be required to retrospectively change an entity's goodwill accounting and to report as though the private company accounting alternatives had not been elected.

4.3 Accounting alternative for evaluating triggering events

In addition to the accounting alternative discussed in Section 4.1, "Amortization of goodwill accounting alternative," the guidance in ASC 350 provides another accounting alternative for nonpublic entities and NFPs that allows them to forego monitoring goodwill impairment triggering events during a reporting period and to instead evaluate these triggering events only as of the end of reporting period, regardless of whether that reporting period is on an interim or annual basis. Said differently, an entity would evaluate goodwill impairment triggering events and measure any related impairment only at the end of each reporting period, and not during the reporting period, using the facts and circumstances that exist at the end of the reporting period.

A nonpublic entity with an interim financial reporting date that elects to apply the accounting alternative must evaluate goodwill triggering events as of the end of each interim reporting period in addition to the end of the annual reporting period.

ASC 350-20-35-84

An entity may elect to perform its goodwill impairment triggering event evaluation only as of the end of each reporting period, whether the reporting period is an interim or annual period. That is, the entity would not evaluate goodwill impairment triggering events and measure any related impairment during the reporting period. An entity electing the accounting alternative shall assess whether events or circumstances have occurred that would require an entity to test goodwill for impairment as follows:

a. For an entity that has elected the accounting alternative for amortizing goodwill, the entity's evaluation of a triggering event, as described in paragraph 350-20-35-66, shall be performed only as of each reporting date.

b. For an entity that has not elected the accounting alternative for amortizing goodwill:

    1. If the entity performs its annual goodwill impairment test as of the end of the reporting period, the entity shall not evaluate its goodwill for impairment during the reporting period as described in paragraph 350-20-35-30.

    2. If the entity performs its annual goodwill impairment test on a date other than the end of the reporting period (in accordance with paragraph 350-20-35-28), the entity's evaluation of impairment between annual goodwill impairment tests (as described in paragraph 350-20-35-30) shall be performed only as of the end of a reporting period.

ASC 350-20-35-85

An entity electing this accounting alternative shall apply it only to goodwill evaluated in accordance with this Subtopic. This accounting alternative does not change the following:

a. The requirement to assess other assets for impairment (for example, long-lived assets and indefinite-lived intangibles) under existing guidance. If the impairment test related to other assets would have resulted in a goodwill impairment triggering event, an entity electing this accounting alternative should consider the results of an impairment test related to other assets in connection with its goodwill impairment test only as of its annual goodwill impairment testing date and the reporting date, whether that date is an interim or annual reporting date, as applicable.

b. The requirements to test the remaining goodwill for impairment if only a portion of goodwill is allocated to a business or nonprofit activity to be disposed of in accordance with paragraph 350-20-40-7.

Under this accounting alternative, certain other requirements under U.S. GAAP remain the same for nonpublic entities, such as the need to assess other assets for impairment—including long-lived assets and indefinite-lived intangible assets—not only at the reporting date but during the reporting period, as well as using the date of the triggering event (which may not be the end of the reporting period) as the measurement date when testing for impairment.

In addition, upon the disposal of a portion of a reporting unit, a nonpublic entity should assess for impairment any portion of goodwill retained as of the disposal date if the relative fair value of goodwill is allocated between the portion of the reporting unit that is disposed of and the portion that is retained.

Grant Thornton insight: Considerations for identifying interim reporting dates when applying the accounting alternative for evaluating triggering events

While the FASB chose not to define what constitutes a “reporting date,” the Board observed in the Basis for Conclusions to ASU 2021-03 that many private companies and NFPs provide some level of financial information that indicates compliance with the recognition and measurement principles in U.S. GAAP—for example, financial information provided to lenders, other investors, or regulators—more frequently than annually. The FASB also observed that when entities provide information compliant with U.S. GAAP on an interim basis, it would be misleading to allow those entities to delay the evaluation of goodwill for impairment until the end of the annual reporting period. Accordingly, if an entity is required (or elects) to provide financial information in compliance with the recognition and measurement principles of U.S. GAAP on an interim basis, the entity should conclude that it has an interim reporting period.

Private entities and NFPs that elect the accounting alternative for evaluating triggering events should carefully review their reporting requirements, including those imposed by debt arrangements, investor agreements, and regulators, to determine whether they are reporting interim financial information in compliance with the recognition and measurement principles of U.S. GAAP. If so, those reporting requirements would create an interim reporting date for purposes of applying the accounting alternative. Additionally, a private entity or NFP should consider whether financial information reported at an interim date would be affected by goodwill impairment when determining whether its reporting requirements create an interim reporting date for purposes of applying the accounting alternative. If the financial information would not be impacted by goodwill impairment, the entity may not have an interim reporting date for purposes of applying the accounting alternative.

Considering whether an entity provides financial information on an interim basis in compliance with the recognition and measurement principles of U.S. GAAP, and determining whether those reporting requirements create an interim reporting date for purposes of applying the accounting alternative, often requires significant judgment.

Nonpublic entity accounting alternative for evaluating triggering events

Scenario 1: Entity has no interim reporting date

During the first quarter of 202X, Entity A, a private entity that has previously adopted the accounting alternative to amortize goodwill under ASC 350-20, now elects to adopt the accounting alternative in ASC 350-20-35-84 to 35-85 for evaluating goodwill impairment triggering events for its 202X financial statements. Entity A determines that it does not have interim reporting periods and has only an annual reporting period.

During the second quarter of 202X, Entity A's main supplier goes out of business, which, absent the adoption of the accounting alternative for evaluating impairment triggering events, would have represented an impairment triggering event in the second quarter. By the fourth quarter of 202X, however, Entity A is able to secure a new supplier with similar terms to the arrangement it had in place with its previous supplier, and cash flows are back in line with its previous forecasts.

Entity A evaluates the facts and circumstances existing as of December 31, 202X (its annual goodwill impairment triggering event evaluation date under the accounting alternative) and concludes that no triggering event exists as of that date. Since Entity A has elected the accounting alternative to amortize goodwill, it is only required to test goodwill for impairment upon the occurrence of a triggering event; since no triggering event has occurred, it is not required to further evaluate goodwill for impairment.

Entity A discloses its election to use the accounting alternative as a significant accounting policy in the notes to the financial statements.

Scenario 2: Entity reports to bank quarterly in compliance with U.S. GAAP

Assume the same facts above, except in this scenario, Entity A provides U.S. GAAP financial statements to its lender at the end of each quarter.

Entity A evaluates the facts and circumstances existing as of the end of each quarterly reporting period in 202X. The entity is required to evaluate whether the loss of its supplier is a triggering event, taking into consideration the facts and circumstances that exist as of June 30, 202X. Entity A determines that a triggering event has occurred as of June 30, 202X and evaluates goodwill for impairment at that date.

The following table compares the guidance for using and not using the goodwill triggering event accounting alternative under ASC 350-20-35-84 to 35-85.

Comparison of guidance with and without goodwill impairment triggering event alternative		
Main provisions	**Requirements without accounting alternative**	**Effect of accounting alternative***
When to evaluate triggering event	At the point in time at which events and circumstances suggest it is more likely than not that goodwill is impaired	Evaluated at each financial reporting date only

*Changes between accounting policies should be preferable in accordance with the guidance in ASC 250. In general, the alternative accounting policies would be less preferrable and, once adopted, would be difficult to "re-adopt" if a company were to reverse its election of any accounting alternatives.

4.4 Identifiable intangible assets accounting alternative

Nonpublic entities may also elect the accounting alternative in ASC 805-20-25-29 through 25-33, which allows them to forego recognizing certain intangible assets separately in connection with a business combination. Under this accounting alternative, the value of certain customer-related and noncompetition intangible assets are subsumed into goodwill. Only noncompetition agreements and customer-related intangible assets that cannot be sold or licensed independently from a business's other assets may be subsumed into goodwill.

A nonpublic entity that elects to apply this accounting alternative must apply it to all future transactions. This accounting alternative is not a transaction-by-transaction election but rather an accounting policy election applicable to all future transactions within the scope of the alternative. Entities that elect to apply this accounting alternative are also required to apply the private company alternative to amortize goodwill, as discussed in Section 4.1, "Amortization of goodwill accounting alternative." However, nonpublic entities that apply the accounting alternative to amortize goodwill are not required to adopt the accounting alternative on subsuming certain customer-related intangible assets and noncompetition-related assets into goodwill.

ASC 805-20-25-29

The guidance in this Subsection applies to entities within the scope of paragraph 805-20-15-2 that elect the accounting alternative for the recognition of identifiable intangible assets acquired in a business combination.

ASC 805-20-25-30

An intangible asset is identifiable if it meets either the separability criterion or the contractual-legal criterion described in the definition of identifiable. However, under the accounting alternative, an acquirer shall not recognize separately from goodwill the following intangible assets:

a. Customer-related intangible assets unless they are capable of being sold or licensed independently from other assets of a business

b. Noncompetition agreements.

ASC 805-20-25-31

Customer-related intangible assets often would not meet criterion (a) in paragraph 805-20-25-30 for recognition. Customer-related intangible assets that would meet that criterion for recognition under this accounting alternative are those that are capable of being sold or licensed independently from the other assets of a business. Examples of customer-related intangible assets are listed in paragraph 805-20-55-20. Many of the customer-related intangible assets that would meet criterion (a) for recognition also would be considered contract-based intangible assets as described in paragraph 805-20-55-31. Customer-related intangible assets that may meet that criterion for recognition include but are not limited to:

a. Mortgage servicing rights

b. Commodity supply contracts

c. Core deposits

d. Customer information (for example, names and contact information).

ASC 805-20-25-32

Contract assets, as used in Topic 606 on revenue from contracts with customers, are not considered to be customer-related intangible assets for purposes of applying this accounting alternative. Therefore, contract assets are not eligible to be subsumed into goodwill and shall be recognized separately.

ASC 805-20-25-33

A lease is not considered to be a customer-related intangible asset for purposes of applying this accounting alternative. Therefore, favorable and unfavorable leases are not eligible to be subsumed into goodwill and shall be recognized separately.

The accounting alternative for identifiable intangible assets applies to the recognition of intangible assets arising from the following in-scope transactions:

- Application of the acquisition method of accounting described in ASC 805
- Assessment of the nature of the difference between the carrying amount of an equity method investment and the underlying equity in net assets of the same equity-method investment, as described in ASC 323
- Adoption of fresh-start reporting, as described in ASC 852

Under the existing guidance in ASC 805, an intangible asset is identifiable—and therefore should be separately recognized—if it is "separable" or "contractual," as defined. However, an entity that elects the identifiable intangible assets accounting alternative should not recognize separately from goodwill identifiable assets that fall into either of the following two categories:

- *Category 1*: Customer-related intangibles, unless they are capable of being sold or licensed independently
- *Category 2:* Noncompetition agreements

If this accounting alternative is elected, customer-related intangible assets should not be recognized apart from goodwill if they cannot be sold or licensed independently from a business's other assets. For purposes of applying this alternative, an identifiable customer-related asset is not capable of being sold or licensed if the asset's sale or license requires any customer action or prior approval. In other words, if a customer must approve an entity's sale of its information, then that asset may not be separately sold under the accounting alternative and would be subsumed into goodwill.

Customer-related intangible assets that can be sold or licensed independently from the other assets of a business, and would therefore be recognized apart from goodwill, include, but are not limited to, the following items:

- Mortgage servicing rights
- Commodity supply contracts
- Core deposits at a financial institution
- Customer information (for example, names and addresses)

Such assets are ineligible to be subsumed into goodwill and will continue to require analysis for separate recognition.

Grant Thornton insight: Valuation considerations for the identifiable intangible assets accounting alternative

The identifiable intangible assets accounting alternative for nonpublic entities was provided to reduce the cost and complexity of measuring certain intangible assets in connection with a business combination. The reduction in cost and complexity of measuring these intangible assets may be greater for certain acquired businesses than for others. The cost savings could potentially be greatest for acquisitions of businesses with acquired intangibles that are limited to these customer-related intangibles or noncompetition agreements. In contrast, there could be little cost savings for acquisitions of businesses that have other intangible assets because many valuation models incorporate contributory asset charges related to the fair value of the customer-related intangible assets or noncompetition agreements into the value of other intangible assets, such as in-process research and development assets or any other intangible asset valued using a multiple-period excess earnings model.

When assigning fair value to the assets acquired and liabilities assumed in a business combination, many valuation specialists perform a reconciliation of discount rates for the individual assets acquired and liabilities assumed compared to the internal rate of return and the market participant weighted-average cost of capital. This type of reconciliation often requires the valuation of an in-place assembled workforce, even though the assembled workforce is subsumed into goodwill and is not separately recognized. Intangible assets subject to this private company alternative are also subsumed into goodwill and require an entity to calculate fair value for these assets in order to perform this type of reconciliation. In these circumstances, there might be little cost savings, even when the acquired intangibles are limited to the customer-related intangibles or noncompetition agreements subject to the alternative.

Reporting entities should take into account these considerations, as well as other insights and challenges discussed in this section, when deciding whether to elect this private company alternative in addition to the required election of the alternative to amortize goodwill based on their specific facts and circumstances.

The following table compares the guidance for using and not using the identifiable intangible alternative, as indicated in ASC 805-20-25-29 to 25-33.

Comparison of guidance with and without identifiable intangible alternative		
Main provisions	**Requirements without accounting alternative**	**Effect of accounting alternative***
Subsuming certain customer-related and noncompete intangibles into goodwill	Not permitted	Required

*Changes between accounting policies should be preferable in accordance with the guidance in ASC 250. In general, the alternative accounting policies would be less preferrable and once adopted would be difficult to “re-adopt” if a company were to reverse its election of any accounting alternatives.

Appendix A: Abbreviations

Abbreviation	FASB Accounting Standards Codification (ASC) or Accounting Standards Update (ASU)
ASC 250	ASC 250, *Accounting Changes and Error Corrections*
ASC 280	ASC 280, *Segment Reporting*
ASC 323	ASC 323, *Investments – Equity Method and Joint Ventures*
ASC 350	ASC 350, *Intangibles – Goodwill and Other*
ASC 350-20	ASC 350-20, *Intangibles – Goodwill and Other - Goodwill*
ASC 350-30	ASC 350-30, *Intangibles – Goodwill and Other – General Intangibles Other than Goodwill*
ASC 360	ASC 360, *Property, Plant and Equipment*
ASC 740	ASC 740, *Income Taxes*
ASC 805	ASC 805, *Business Combinations*
ASC 842	ASC 842, *Leases*
ASC 852	ASC 852, *Reorganizations*
ASU 2017-04	ASU 2017-04, *Simplifying the Test for Goodwill Impairment*
ASU 2021-03	ASU 2021-03, *Accounting for Evaluating Triggering Events*

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