

June 22, 2016

Technical Director
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File Reference No. 2016-230

Proposed Accounting Standards Update: Intangibles—Goodwill and Other (Topic 350)
Simplifying the Accounting for Goodwill Impairment

The Accounting Principles and Assurance Services Committee (the “Committee”) of the California Society of Certified Public Accountants (“CalCPA”) respectfully submits its comments on the referenced proposals. The Committee is the senior technical committee of CalCPA. CalCPA has approximately 43,000 members. The Committee consists of 57 members, of whom 43 percent are from local or regional CPA firms, 30 percent are from large multi-office CPA firms, 13 percent are sole practitioners in public practice, 9 percent are in academia and 5 percent are in international CPA firms. Members of the Committee are with CPA firms serving a large number of public and nonpublic business entities, as well as many non-business entities such as not-for-profits, pension plans and governmental organizations.

The Committee supports the amendments in the proposed Update. They improve evaluating and accounting for goodwill impairment by substantially simplifying the requirements.

Question 1: Do you agree with the proposed amendments to eliminate Step 2 from the goodwill impairment test? Why or why not?

The Committee agrees with the proposed amendments to eliminate Step 2 from the goodwill impairment test. The proposed amendments will substantially simplify the accounting requirements for evaluating potential impairment of goodwill.

Question 2: Should the requirement to perform Step 2 of the current goodwill impairment test be retained as an option? Why or why not? If the use of Step 2 is optional, should an entity be allowed to apply that option by reporting unit or should it be a policy election at the entity level applicable to all reporting units?

The Committee generally favors consistent accounting for the same transactions across all entities, so it does not believe Step 2 of the current goodwill impairment test should be retained as an option. However, if the Board does decide to retain it as an option, the Committee believes it should be applied at the reporting unit level, and the impairment loss recognized should not be less than that which would be recognized under the proposed amendments.

Question 3: Do you agree with the proposed amendments to require all entities to apply the same one-step impairment test to all reporting units, including those with zero or negative

carrying amounts? Why or why not? If not, what would be the suggested goodwill impairment test for reporting units with zero or negative carrying amounts?

While the proposed amendments would simplify the impairment test for reporting units with zero or negative carrying amounts, the Committee is concerned that any goodwill in this situation would often escape evaluation for impairment since it would be unusual for a reporting entity to have a negative fair value. A zero or negative carrying value is often the result of operating losses and other negative factors described in ASU Topic 350, paragraph 350-20-35-3C and these may create a *prima facie* need to record impairment. The accounting standards should require a rigorous evaluation of goodwill impairment in this situation, and not condone ignoring it and relegating the issue to a disclosure which may never be read. The Board stated that its staff found few cases of reporting units with zero or negative carrying amounts. If that is the case, it should not be burdensome to apply a different test to such entities. The Committee observes that a test similar to that in Step 2 may not be adequate because, since it would be rare for a reporting unit to have a negative fair value, there is a likelihood that a purchase price type allocation required by Step 2 may give rise to an unidentifiable “excess cost” (i.e., goodwill) not indicative of any real value.

The Committee recognizes that the Basis for Conclusions in the proposed ASU reflects that the Board struggled with this issue. We doubt that there is a theoretical way to apply the Board’s proposed basic accounting model to these situations. That is not a reason to not use the model, but is a reason to prescribe different accounting for these unusual situations. Of the alternatives discussed in the Basis for Conclusions, a rebuttable presumption that goodwill is impaired for reporting units with zero or negative carrying amounts, seemed to the Committee to be the most workable, although admittedly not perfect. While it may be costly and complex for an entity choosing to rebut the presumption, it seems that these situations are sufficiently uncommon that the benefit of avoiding situations where obvious impairment is not recognized is worth the cost.

Question 4: Should entities with reporting units with zero or negative carrying amounts be required to disclose the existence of those reporting units and the amount of goodwill allocated to them? Why or why not? Are there additional disclosures that would provide useful information to users of financial statements?

The Committee is not sure of the point of such disclosures. If the accounting is appropriate, then goodwill in reporting units with zero or negative carrying amounts should need no separate disclosure. If the disclosure is because the proposed accounting leaves the risk of loss for goodwill in such reporting units as high, then the better answer is to fix the accounting. See response to Question 3.

Question 5: Should the guidance on deferred income tax considerations when determining the fair value of a reporting unit outlined in paragraphs 350-20-35-25 through 35-27 and illustrated in Example 1 and Example 2 be retained, or should this Subtopic rely on the fair value guidance in Topic 820, Fair Value Measurement? If the guidance on the tax structure is retained, what, if any, amendments are necessary to address the potential difference in the impairment charge calculated under the proposed amendments, depending on which tax structure is used in calculating the fair value of the reporting unit?

The Committee believes that the guidance on deferred income tax considerations when determining the fair value of a reporting unit outlined in paragraphs 350-20-35-25 through 35-27 is useful in determining fair value and should therefore be retained.

The potential difference in the impairment charge calculated under the proposed amendments, depending on which tax structure is used in calculating the fair value of the reporting unit, is not a new issue, but one that would be encountered under the existing requirements. The basic issues seem to be identified, and in the absence of specific concerns of the Board, we have no further comment.

Question 6: Do you agree that the proposed guidance to remove Step 2 from the goodwill impairment test should be applied prospectively? Should there be specific transition guidance for companies that previously adopted the goodwill accounting alternative for private companies in current GAAP but decide to adopt this proposed guidance after it becomes effective?

The Committee agrees that the proposed guidance to remove Step 2 from the goodwill impairment test should be applied prospectively. It would not be feasible to apply it retrospectively.

Entities that have adopted the goodwill accounting alternative for private companies in current GAAP should not have the option to adopt this proposed guidance after it becomes effective for goodwill that is being amortized pursuant to that option. The practical effect of adopting the proposal would be that the impairment evaluation would change slightly, but the amortization of goodwill over no more than ten years may no longer be required. The reduction or avoidance of future goodwill amortization for goodwill already being amortized strikes the Committee as inappropriately manipulative. However, the Committee would have no objection to affording such entities the option to apply the proposed guidance to amortization of goodwill arising after the effective date of the proposal if the entity.

Question 7: How much time would be necessary to adopt the amendments in this proposed Update? Should early adoption be permitted? Would the amount of time needed to apply the proposed amendments by entities other than public business entities be different from the amount of time needed by public business entities?

The Committee does not know how much time would be necessary to adopt the amendments in this proposed Update, but believes that it would be less than that to apply existing guidance. The time to transition to the new guidance should be minimal, since it is simpler to apply than existing guidance. Similarly, time to transition for non-public entities, assuming that they are not using the optional accounting available to non-public entities, should be less than that required to continue to apply existing guidance for public entities.

Question 8: Would the proposed amendments meet the Board's objective of reducing the cost of the subsequent accounting for goodwill while maintaining the usefulness of the information provided to users of financial statements? Why or why not?

The Committee believes that the proposed amendments meet the Board's objective of reducing the cost of the subsequent accounting for goodwill while maintaining the usefulness of the information provided to users of financial statements.

Question 9: Are there additional changes that should be made to the subsequent accounting for goodwill to meet this objective, including changes that might be considered in Phase 2 of the Board's project?

The Committee suggests that the proposed changes in Phase 1 of the Board's consideration of accounting for goodwill are adequate and the results of the implementation of the guidance should be studied before any further changes in evaluation of impairment. The Committee encourages the Board to consider whether to make additional changes to the subsequent accounting for goodwill, including consideration of permitting or requiring amortization of goodwill.

Question 10: Are there any unintended consequences resulting from the improvements to the Overview and Background Sections of the Subtopics (discussed in Part II of the proposed amendments)?

The Committee does not foresee any unintended consequences resulting from the improvements to the Overview and Background Sections of the Subtopics

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We thank you for the opportunity to comment on this matter. We would be glad to discuss our opinions with you further should you have any questions or require additional information.

Sincerely,

A handwritten signature in black ink, appearing to read 'A.J. Major III', with a horizontal line underneath the name.

A.J. Major III
Chair
Accounting Principles and Assurance Services Committee
California Society of Certified Public Accountants