CNM LLP
Technical Advisory Firm

September 30, 2019

Mr. Shane Kuhaneck
Acting Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Re: File Reference No. 2019-720—Invitation to Comment, Identifiable Intangible Assets and Subsequent Accounting for Goodwill

Dear Mr. Kuhaneck:

CNM LLP is an accounting advisory firm based in Southern California. We would like to thank you for the opportunity to comment on the accounting for identifiable intangible assets and subsequent accounting for goodwill. We believe that certain changes to the accounting for identifiable intangible assets and the subsequent accounting for goodwill would be cost beneficial to public companies and provide more meaningful and transparent financial information to users of their financial statements. Our comments on the questions posed to respondents are expressed below.

Section 1: Whether to Change the Subsequent Accounting for Goodwill

1. What is goodwill, or in your experience what does goodwill mainly represent?

We believe that goodwill is a premium paid by an acquirer for an acquiree over and above the fair value of the identifiable net assets acquired. Presumably, the acquirer is willing to pay this premium because it believes that there is additional intangible value (e.g., synergy or strategic value) associated with merging the acquiree's business with its business and operations that cannot be attributed to an identifiable tangible or intangible asset. That additional value is expected to result in higher revenues, reduced costs, or higher profit margins over some future period that at least equals the premium paid. This strategic value also could be attributed to a defensive measure to protect a public company's market share or acquiring certain technology that it currently does not possess.

2. *Do the benefits of the information provided by the current goodwill impairment model justify the cost of providing that information?*

Although the current goodwill impairment model does provide some useful information to users of financial statements, we believe that there are alternative approaches that would be more cost beneficial (e.g., amortization over the expected benefit period). While an impairment approach is beneficial when amortization is not allowed, we believe that the current model commingles the acquired goodwill with subsequently generated internal goodwill, which is inconsistent with the notion that internally generated intangible assets are not capitalized. As a result, the current impairment model does not provide a true picture of the value actually provided by the acquired goodwill that would allow users of financial statement to assess whether the premium paid to acquire the target company was worth the cost.

3. *On a cost-benefit basis, relative to the current impairment-only model, do you support (or oppose) goodwill amortization with impairment testing?*

We believe that goodwill amortization over the estimated useful life of the goodwill better reflects the economics of the business combination transaction and, therefore, would provide more meaningful information to users of financial statements. We believe that acquired goodwill has a finite life and does not continue to provide benefits forever or an extended period of time. Rather, its value is gradually replaced by goodwill that is internally generated by the merged companies. Using internally generated goodwill to support the notion that the acquired goodwill has not diminished in value is misleading and does not allow users of financial statements to assess how beneficial the added premium paid in an acquisition was to the acquirer.

Because events can occur that accelerate the decline in value of acquired goodwill, an impairment assessment is needed similar to any other long-lived asset to ensure that recorded investment outstanding is recoverable as of each reporting date when there are indications that the recorded investment in the goodwill asset might be impaired.

4. *If the Board were to decide to amortize goodwill, which amortization period characteristics would you support?*

We believe that goodwill should be amortized over (g) Management's reasonable estimate of the period over which the acquired goodwill will benefit the merged company. While that period might be difficult to estimate in certain circumstances, we believe that such an estimation would be no more difficult than other difficult estimates required in other accounting standards (e.g., ASC 326 or ASC 740).

We believe that a default period, a cap, or a floor have no conceptual basis and would not be better measures of goodwill amortization or provide more meaningful information to users of financial statements. Such approaches should be used only as practical expedients if the Board were to decide that the cost of estimating the useful life of goodwill outweighed the benefits in certain situations.

With regard to amortization periods based on the useful life of the primary identifiable asset acquired or a weighted-average of useful lives of identifiable assets acquired, while we believe that these represent measurement techniques that could be used by Management to estimate the useful life of goodwill, they should not preclude Management from using other estimation techniques that are deemed appropriate in the circumstances.

5. *Do your views on amortization versus impairment of goodwill depend on the amortization method and/or period?*

We believe that amortization of goodwill over its estimated life is the best approach that reflects the economics of the acquisition transaction. The amortization method and/or period should not be the primary consideration. Nevertheless, we believe that in most cases, the useful life of goodwill over a prolonged period without consideration of subsequently generated goodwill will not be supportable, as an entity's ability to forecast future earnings over a prolonged period is limited.

We acknowledge that using a practical expedient can be cost beneficial (by reducing the costs of application) and makes the reported financial results more comparable between different companies. Nevertheless, when practical expedients are applied to goodwill amortization, the benefits are diminished, as the resulting amortization no longer will reflect the actual results. Practical expedients are blunt instruments or shortcuts that provide less meaningful information for the sake of reduced cost or complexity. Depending on how blunt those practical expedients are designed will determine whether such an approach is an improvement to or worse than the current impairment approach. For example, goodwill amortization over a default period that is a very short (e.g., two-year) or long (e.g., 40-year) period is not likely to improve the information provided as compared to the current impairment approach.

6. *Regarding the goodwill amortization period, would equity investors receive decision-useful information when an entity justifies an amortization period other than a default period? If so, does the benefit of this information justify the cost?*

We believe that using management's best estimate of the amortization period will always produce superior results compared to a default period, which in turn will provide more decision-useful information to investors and other users of financial statements. When an acquirer negotiates the purchase price of an acquired company, in order to make an intelligent bid, the acquirer must consider the return on investment (ROI) expected from the premium in excess of the estimated fair value of the net assets acquired. The calculation of that ROI also requires an assumption about the payback period over which the acquirer wants to measure its ROI from the transaction. As such, the amortization applied would give investors insights on the period over which the premium paid is expected to generate a return, which would allow an investor to assess whether the entity made a good (or bad) decision in negotiating the purchase price.

In most cases, we believe that in determining a purchase price, an acquirer should have at least a rough idea of an estimated period or target time horizon from which it expects or hopes to derive most of the benefits from the premium paid. In that case, it should not be impractical for an acquirer to estimate a period over which to amortize the goodwill. Based on the insights gained from being able to observe the return generated from the premium paid, we believe that the benefits would more than justify the cost involved. Subsequently, as the acquirer observes the actual results from the acquisition, the estimated amortization period can be refined and improved.

7. *Do the amendments in Update 2017-04 (eliminating Step 2 of the goodwill impairment test) reduce the cost to perform the goodwill impairment test? Do the amendments in Update 2017-04 reduce the usefulness of financial reporting for users?*

We believe that the elimination of Step 2 reduces the cost significantly when a quantitative analysis is required to determine whether the recorded goodwill is impaired. Furthermore, we believe that the benefits from Step 2 did not significantly outweigh the costs of performing that step. We believe that while users do want to know that the goodwill recorded on the balance sheet is not impaired, they do not benefit significantly from complex measurement methods to make that determination, especially when that measurement relies heavily on estimates and assumptions. We believe that users only want to know that the recorded goodwill is not materially misstated, as goodwill does not affect the cash flows or operations of the reporting entity.

8. *Do the amendments in Update 2011-08 (qualitative screen) reduce the cost to perform the goodwill impairment test? Do the amendments in Update 2011-08 reduce the usefulness of financial reporting information for users?*

We believe that the use of a qualitative screen significantly reduces the cost to perform the goodwill impairment test, as in many cases it is evident that the recorded goodwill, which is buoyed by subsequently generated internal goodwill, is not impaired under common conditions (e.g., sustained or increased stock price, historical and forecast profitability, strong business and economic conditions, sustained or increased revenues, sustained or lower operating costs, and stable business).

The amendments in Update 2011-08 do not reduce the usefulness of financial reporting information for users because significant impairment continues to be identified on a timely basis and users are primarily concerned that there is no material overstatement in the recorded goodwill, as goodwill does not impact cash flows or the operations of the reporting entity.

9. Relative to the current impairment model, how much do you support (or oppose) removing the requirement to assess goodwill (qualitatively or quantitatively) for impairment at least annually?

We would oppose removing the requirement to assess goodwill (qualitatively or quantitatively) at least annually. Because goodwill is deemed to have an indefinite life under the current model, we believe that it is important assess whether goodwill is impaired at least annually to ensure that the recorded investment is not overstated in the financial statements at year-end. We believe that goodwill created in a business combination diminishes in value over time. In the absence of amortization, the only way to recognize a decline in the recorded goodwill is through impairment. In that case, a periodic assessment of goodwill impairment is necessary to ensure that any decrease in value of goodwill is captured on a timely basis.

10. Relative to the current impairment model, how much do you support (or oppose) providing an option to test goodwill at the entity level (or at a level other than the reporting unit)?

We do not support an option to test goodwill at the entity level, as we do not believe that testing goodwill at the reporting unit level provides a significant benefit to financial statement users. The testing of goodwill impairment should remain at the reporting unit level. If impairment is measured at the entity level, it commingles the value of acquired goodwill with internally generated goodwill. While it is difficult to distinguish how internally generated goodwill should be allocated to the reporting units, providing an entity with the ability to use internally generated goodwill from all its operations in the impairment measurement related to a specific reporting unit, masks the realization of the goodwill to which it is applicable. We believe that financial statement users are most concerned with whether the recorded investment in goodwill to which reporting unit it is applicable is impaired.

11. What other changes to the impairment test could the Board consider?

We believe that no other changes to the impairment test need to be considered at this time.

12. *Please indicate whether you support the following alternatives by answering "yes" or "no" to the questions in the table below.*

	Do you Support the Indicated Model? Yes/No	Do You Support Requiring an Impairment Assessment Only upon a Triggering Event? Yes/No	Do You Support Allowing Testing at the Entity Level or a Level Other Than the Reporting Unit? Yes/No
Impairment only	No	No	No
Amortization with impairment	Yes	Yes	Yes
Amortization only	No	Not applicable	Not applicable

Section 2: Whether to Modify the Recognition of Intangible Assets in a Business Combination

13. *Please describe what, if any, cost savings would be achieved if certain recognized intangible assets (for example, noncompete agreements or certain customer-related intangible assets) were subsumed into goodwill and amortized. For example, include specific purchase price allocation or subsequent accounting cost savings. Please list any additional intangible items the Board should consider subsuming into goodwill.*

We believe that the primary cost savings if certain intangible assets were subsumed into goodwill and amortized would stem from the elimination of the need to estimate the acquisition date fair value. Many companies do not have internal resources with the skill set necessary to estimate those fair values and must hire external consultants to perform the valuations, which can cost several thousands of dollars.

We believe that the subsequent amortization costs would be similar in this situation, as most commonly recognized intangible assets have finite lives over which they are already being amortized and are subject to impairment assessment when there is an indication that the recorded investment might be impaired. This effort would not be significantly different if they were subsumed in goodwill and amortized. The cost of amortizing a single intangible asset (goodwill) instead of multiple intangible assets might be slightly less but the savings probably would not be significant.

14. *Please describe what, if any, decision-useful information would be lost if certain recognized intangible assets (for example, noncompete agreements or certain customer-related intangible assets, or other items) were subsumed into goodwill and amortized.*

We believe that there could be some loss of decision-useful information if certain recognized intangible assets were subsumed into goodwill and amortized, depending on whether there are significant differences in the estimated benefit (amortization) period. We believe that these intangible assets, like acquired goodwill, have diminishing value over time and should be amortized over their estimated benefit period. If there is no significant difference in the amortization periods, we do not believe that users of financial statements derive significant benefit from having certain recognized intangible assets recorded separately, as they often are reported in the same line item in the financial statements and do not directly impact the operations or cash flows of the entity. We believe that a requirement to disclose the types identifiable intangible assets subsumed in goodwill would be sufficient to give users of financial statements an understanding of why the acquirer paid a premium over the fair value of the separately recorded net assets acquired. Nevertheless, if entities are permitted to subsume certain intangible assets in goodwill, then we believe that a reporting entity should not be precluded from recording and amortizing identifiable intangible assets separately from goodwill if they so desire in order to provide more transparency.

15. *How reliable is the measurement of certain recognized intangible assets (for example, noncompete agreements or certain customer-related intangible assets)?*

Generally, intangible assets recognized in an acquisition have no readily observable market prices or market trades of similar assets. As such, their fair value must be estimated using valuation techniques (e.g., net present value of future expected cash flows). Because those valuation techniques require at least one significant unobservable input or assumption, they generally are Level 3 fair value measurement under FASB Accounting Standards Codification Topic 820, *Fair-Value Measurement*. Furthermore, such valuations require a significant liquidity premium for uncertainty and illiquidity, which is difficult to ascertain without observable market transactions. We believe that the estimated fair value is subjective and usually is selected from a broad range of possible estimates. Nevertheless, accounting estimates are a core foundation of the preparation of financial statements and financial reporting. Disclosure of the significant assumptions used to measure the values assigned to the intangible assets and the level of sensitivity or variability from changes in those assumptions would be critical to helping users assess the reasonableness of those estimates.

16. *To gauge the market activity, are you aware of instances in which any recognized intangible assets are sold outside a business acquisition? If so, how often does this occur?*

In our experience, most of the types of intangible assets being discussed (e.g., noncompete agreements or customer-related intangible assets) are not sold individually. In business today, information is extremely valuable, and we suspect that customer information and consumer data is being sold and or licensed regularly. However, the prices of such transactions may not be readily observable.

17. *Of the possible approaches presented, which would you support on a cost-benefit basis? Please rank the approaches (1 representing the most preferable approach) and explain why you may not have selected certain approaches.*

We would rank the four presented approaches as follows:

1. Approach 2: Apply a Principles-Based Criterion for Intangible Assets
2. Approach 1: Extend the Private Company Alternative to Subsume Certain CRIs and all NCAs into Goodwill
3. Approach 4: Do not Amend the Existing Guidance
4. Approach 3: Subsume All Intangible Assets into Goodwill

Of the four approaches presented, we believe that the costliest alternative would be Approach 4, which would make no changes to the current prescribed accounting. Consequently, we believe that Approaches 1-3 would be less costly to apply to varying degrees.

We believe that Approach 2 would provide the most beneficial information to financial statement users. Certain types of intangible assets, especially those that are contractually based (e.g., mortgage servicing assets, patents, and licenses), have identified value that impacts the future cash flows of the reporting entity. Separately identifying and amortizing such intangible assets over their estimated benefit period (subject to an impairment assessment if indicators are observed) would provide financial statement users with the most transparent and useful information. We believe that this approach would be less costly than Approaches 1 and 4, as fewer intangible assets would be required to be separately recognized and amortized. Furthermore, this approach would provide significantly more useful and transparent information than Approach 3.

We believe that Approach 1 would require more intangible assets to be recognized for which the costs would outweigh the benefits. We also believe that Approach 3 would require too few intangible assets to be recognized and would result in significantly less useful information and transparency.

18. *As it relates to Approach 2 (a principles-based criterion), please comment on the operability of recognizing intangible assets based, in part, on assessing whether they meet the asset definition.*

We believe that Approach 2 would be operationally feasible and no more complex to apply in practice than the current accounting that already is being applied to intangible assets recognized in a business combination. Approach 2 could be made operationally easier if that approach limited recognition of intangible assets to those that are contractual in nature (e.g., servicing rights, patents, and licenses).

19. *Approaches 1-3 assume that subsuming additional items into goodwill would necessitate the amortization of goodwill. Do you agree or disagree?*

Yes. We believe that subsuming intangible assets into goodwill necessitates the amortization of goodwill. Otherwise, the decline in value of such intangible assets with finite lives could be offset by internally generated goodwill and not recognized on a timely basis under the current impairment approach.

Section 3—Whether to Add or Change Disclosures about Goodwill and Intangible Assets

20. *What is your assessment of the incremental costs and benefits of disclosing the facts and circumstances that led to impairment testing that have not led to a goodwill impairment loss?*

In practice, we believe that disclosing detailed information regarding goodwill impairment testing (other than the annually required assessment) that does not result in the recognition of an impairment loss would be ignored by most readers of financial statements. Although the costs of such disclosure would not be significant and providing key assumptions used in the impairment assessment would provide greater transparency, we are not confident that benefits would outweigh the costs. We believe that financial statement users are concerned mainly with any significant overstatement of the recorded goodwill balance. While providing more information seems like a benefit to financial statement users, we have concerns that users are becoming overloaded with information that does not provide significant insights into the company's financial condition or performance. In other words, at some point, extraneous information starts to become a distraction from important information.

21. *What other, operable ideas about new or enhanced disclosures would you suggest the Board to consider related to goodwill?*

We believe that companies should disclose the time horizon over which the recorded investment in goodwill is expected to provide value to their operations with a description of that value is expected to be realized.

22. *What is your assessment of the incremental costs and benefits of disclosing quantitative and qualitative information about the agreements underpinning material intangible items in (a) the period of the acquisition and (b) any changes to those agreements for several years post-acquisition?*

We believe that qualitative information about agreements underlying material intangible assets in the period of acquisition would provide useful information to financial statement users. This would be true especially if certain intangible assets are subsumed in goodwill. Since the fair value measurement of material intangible assets (that are not covered by other guidance) generally will involve significant assumptions, projections, and judgment, we do not believe that quantitative information would be very meaningful to financial statement users.

For subsequent periods, we believe that disclosure of changes to such agreements should be required only when they have a significant impact on the recorded investment. Otherwise, we do not believe that disclosure of changes to the agreements would provide meaningful or decision-useful information.

23. *Are there other changes (deletions and/or additions) to the current disclosure requirements for goodwill or intangible items that the Board should consider?*

We believe that companies should disclose the time horizon over which the recorded investment in goodwill is expected to provide value to their operations with a description of that value is expected to be realized.

Section 4: Comparability and Scope

24. *Under current GAAP, to what extent does noncomparability in the accounting for goodwill and certain recognized intangible assets between PBEs and private business entities and not-for-profit entities reduce the usefulness of financial reporting information?*

We believe that the basic premise for divergence in accounting standards between PBEs and other entities is that non-PBEs generally do not compete with PBEs, are smaller in size with relatively few investors, and the benefits of more transparent accounting do not outweigh the costs for such entities. In most cases, we believe that presumption is true. In that case, we do not believe that differences that are relatively small in nature do not significantly reduce the usefulness of financial information presented by non-PBEs.

25. Please describe the implications on costs and benefits of providing PBEs with an option on how to account for goodwill and intangible assets and the option for the method and frequency of impairment testing (described previously in Section 1 and 2).

We do not support providing PBEs with an option on how to account for goodwill and intangible assets or the method and frequency of impairment testing. We believe that providing such options, significantly reduces the benefits because of the total lack of comparability between PBEs. Consequently, any cost savings would not outweigh the significant reduction in benefits. We also believe that providing an open choice to PBEs has no conceptual basis and would lead to greater diversity in practice.

26. To what extent does noncomparability in the accounting for goodwill and certain recognized intangible assets between PBEs reporting under GAAP and PBEs reporting under IFRS reduce the usefulness of financial reporting information?

Obviously, noncomparability in the accounting for goodwill and certain recognized intangible assets between PBEs reporting under GAAP versus IFRS reduces the usefulness of financial information reported under IFRS. Nevertheless, we believe that convergence should not be an overriding factor in setting GAAP. Rather, convergence should be just one factor to consider when equally acceptable approaches are determined under GAAP.

27. Please indicate the sources of comparability that are most important to you regarding goodwill and intangible assets. Please select all that apply and explain why comparability is not important to you in certain cases.

a. Comparability among all entities reporting under GAAP (one requirement for PBEs, private business entities, and not-for-profit entities)
b. Comparability among all PBEs reporting under GAAP
c. Comparability among all private business entities and all not-for-profit entities reporting under GAAP
d. Comparability among all PBEs reporting under GAAP and PBEs reporting under IFRS.

Ideally, we believe that the goal of accounting standards should be to provide comparability among all entities reporting under GAAP (one requirement for PBEs, private business entities, and not-for-profit entities). In that case, the source of comparability that is most important to us regarding goodwill and intangible assets is:

a. *Comparability among all entities reporting under GAAP (one requirement for PBEs, private business entities, and not-for-profit entities)*

While that should be the goal, we acknowledge that in some cases, the cost of providing comparability between PBEs and non-PBEs in this particular case might outweigh the benefits. Therefore, for certain intangible assets, we believe that it would be acceptable for non-PBEs to subsume them into goodwill rather than identify, measure, and record them separately. However, non-PBEs should not be precluded from identifying and recording intangible assets that are contractual in nature (e.g., servicing rights, a patent, or a license).

In addition, we believe that comparability between PBEs reporting under GAAP and those reporting under IFRS are of less importance. We do not support adopting an accounting standard for goodwill and intangible assets that is primarily based on IFRS for the sake of comparability. We believe that the U.S. capital markets, economy, and business practices are significantly different from many foreign countries. While the notion of a single uniform set of accounting standards for the entire world is a noble thought, such a notion is not practical because of those differences. Each country has its own governing concepts that impact its economy and differ from other countries, which in turn means that a single set of accounting standards can fit every situation. As the U.S. capital markets are one of, if not the, best in the world, we believe that U.S. GAAP should not adopt an inferior accounting standard just for the sake of comparability with IFRS.

Other Topics for Consideration

28. Do you have any comments related to the Other Topics for Consideration Section or other general comments?

We support the conclusions reached in the section on Other Topics for Consideration. We believe that there is no need to reconsider whether goodwill and certain other intangibles should be recognized as assets. Our understanding is that there are no significant objections in practice to recording assets for goodwill and certain other intangibles. In that case, we believe the Board should focus on the subsequent measurement of those assets.

We agree with the notion that an immediate write-off of goodwill should not be considered, as it does not reflect the economics of the related business combination transaction. The acquirer pays a premium for an acquired company because it believes that the combination will result in future returns that achieve at least an expected level, which cannot be assigned to any specifically identified asset. For example, greater efficiencies and economies of scale that result in lower operating costs or generate higher revenues or reduced risk from adverse changes in the economic or competitive environment.

Lastly, we support the current accounting for recognizing deferred taxes related to goodwill depending on whether the temporary difference is expected to qualify for a tax deduction in the future.

Next Steps

29. Would you be interested and able to participate in the roundtable?

We would be interested and available to discuss our comments in the roundtable.

Very truly yours,

Lawrence Gee

Lawrence Gee
Professional Practice Director
CNM LLP