Defining Issues®

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Contents

FASB Issues Private Company Alternative to Account for Identifiable Intangible Assets

The FASB and Private Company Council (PCC) recently issued guidance that gives private companies an alternative to include certain identifiable intangible assets in goodwill when applying purchase accounting in business combinations.[1]

All entities other than public business entities, not-for-profit entities, and certain employee benefit plans can elect the alternative.[2]

Key Facts

- A private company electing the alternative will not separately recognize (a) certain customer-related intangible assets and (b) noncompetition agreements when applying purchase accounting and in certain other limited circumstances. This election also requires the private company to amortize goodwill under the previously issued goodwill alternative.[3]
- The guidance is effective prospectively for in-scope transactions occurring in the first annual period beginning after December 15, 2015. Early adoption is allowed.

Key Impacts

- Some private companies will separately account for fewer intangible assets for future business combinations, which could reduce comparability among companies.
- Early adoption allows a private company to apply the alternative to in-scope transactions that occurred in 2014 if the related financial statements have not yet been made available for issuance.

[1] FASB Accounting Standards Update No. 2014-18, Accounting for Identifiable Intangible Assets in a Business Combination, available at www.fasb.org.

[2] Employee benefit plans within the scope of FASB ASC Topics 960 through 965 cannot apply the alternative. For information on the FASB's definition of a public business entity, see KPMG's Defining Issues No. 14-7, FASB Issues New Private Company Guidance, available at www.kpmginstitutes.com/financial-reporting-network.

[3] FASB Accounting Standards Update No. 2014-02, Accounting for Goodwill, available at www.fasb.org.

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Why Revisit the Accounting for Business Combinations?

Current U.S. GAAP generally requires an acquirer to recognize separately from goodwill the identifiable assets acquired, liabilities assumed, and any noncontrolling interest in the acquiree, and to measure these items at their acquisition date fair value.

The PCC and FASB heard from private company stakeholders that the benefits of separately accounting for certain intangible assets acquired in a business combination may not justify the related cost and complexity particularly for estimating the fair value of intangible assets that do not generate cash flows independent of the other assets of the business. The FASB provided this alternative to address those concerns.

How Do I Apply the Alternative?

Customer-related Intangibles and Non-competition Agreements. A private company electing the accounting alternative will apply it to all in-scope transactions entered into after the effective date. A private company may use the alternative when:

- Applying the acquisition method for a business combination;[4]
- Assessing the nature of the difference between the carrying amount of an investment and the amount of underlying equity in net assets of an equity method investee;[5] and
- Adopting fresh-start reporting when emerging from a Chapter 11 reorganization action.[6]

In electing the alternative, a private company will not recognize separately from goodwill the following intangible assets:

- Customer-related intangible assets, unless they are capable of being sold or licensed independently from the other business assets; and
- Noncompetition agreements.

While many customer-related intangible assets are not capable of being sold or licensed independently, often those that can be are considered contract-related intangibles. Examples of customer-related intangible assets that may require separate recognition (i.e., are not eligible for the alternative) include mortgage servicing rights, commodity supply contracts, core deposits, and customer information. The PCC and FASB concluded that whether a customer-related intangible is capable of being sold or licensed independently generally will be apparent based on whether the private company can transfer the intangible without involvement or approval from the customer. Intangibles that can be freely transferred without customer involvement generally would require separate recognition.

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[4] FASB ASC Topic 805, Business Combinations, available at www.fasb.org.

[5] FASB ASC Topic 323, Investments—Equity Method and Joint Ventures, available at www.fasb.org.

[6] FASB ASC Topic 852, Reorganizations, available at www.fasb.org.

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The following are not considered customer-related intangible assets for purposes of applying the alternative (and therefore should be recognized separately from goodwill):

- Contract assets recognized in revenue transactions with customers,[7] and
- Leases, including favorable and unfavorable lease intangibles.

Customer-related intangibles and noncompetition agreements that exist as of the beginning of the period of adoption should continue to be subsequently measured based on existing GAAP (i.e., they should not be subsumed into goodwill upon adoption).[8]

Goodwill. Electing the accounting alternative also requires the private company to amortize goodwill under the previously issued goodwill alternative. New goodwill (including the customer-related intangibles and noncompetition agreements that are not recognized separately under the alternative) arising as a result of an in-scope transaction must 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). Existing goodwill associated with previous transactions also should be amortized prospectively as of the adoption of this alternative.

Disclosure. Private companies electing the alternative should refer to the current disclosure requirements for intangibles that do not require separate recognition in business combinations. These companies also should consider disclosing the application of the alternative as an accounting policy election.

Transition and Effective Date. A private company must elect the alternative upon the occurrence of the first in-scope transaction in its first fiscal year beginning after December 15, 2015. If the first transaction occurs in the first fiscal year beginning after December 15, 2015, then the date of adoption is considered to be that fiscal year's financial statements and interim periods and annual periods thereafter. If the first transaction occurs in the fiscal year beginning after December 15, 2016, then the date of adoption is considered the interim period that includes the date of the transaction and subsequent interim and annual periods thereafter. Early adoption allows a private company to apply the alternative to business combinations completed in 2014 if those financial statements have not yet been made available for issuance.

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[7] FASB Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers, available at www.fasb.org.

[8] FASB ASC Topic 350, Intangibles—Goodwill and Other, available at www.fasb.org.

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