Things to Consider

Goodwill Impairment Testing

Goodwill represents the excess of the cost of an acquired entity over the net of the amounts ascribed to its recognized assets and liabilities. Following initial recognition through purchase accounting, goodwill is tested for impairment under ASC 350 at least annually, or upon the occurrence of a triggering event.

At Tall Oaks Partners, we understand and appreciate the importance of having a quality and supportable valuation for goodwill impairment testing purposes. Here are six things to consider when preparing your valuation estimates:

- **Forecast** – Analyze the company's forecast to confirm that it accounts for a full business cycle and that the terminal period cash-flow is representative of a "normalized" level of revenue, profit margin, and capital spending. As a reasonableness check, implied multiples and other metrics can be calculated to help evaluate the overall forecast, terminal cash-flow assumptions, and key valuation inputs being used in the income approach analysis.
- **Methodology Selection** – Consider each of the primary approaches to value, including the income approach, market approach, and cost approach. Most commonly, for a goodwill impairment test a combination of the income and market approaches would be used to estimate the fair value of a reporting unit.
- **Allocations** – Identify any assets, liabilities, or expenses that may be employed in or related to the operations of multiple reporting units or held at the corporate level and determine if they need to be allocated. The methodology used to allocate amounts to each reporting unit in these cases should be reasonable, supportable, and applied in a consistent manner[1].
- **Other Assets and Liabilities** – Review and discuss the reporting unit and associated consolidated company balance sheets to identify any assets and/or liabilities that need to be separately accounted for in the valuation analysis to properly reflect the value of the reporting unit (e.g., off-balance-sheet items, excess working capital, derivatives, deferred taxes).
- **Reconciliation** – For publicly traded companies, prepare a market capitalization reconciliation to support the fair values estimated for the subject reporting unit(s). This reconciliation may be more complex for companies with multiple lines of business and/or reporting units.
- **Documentation** – Detail the approaches/methods and steps considered and selected in estimating the value of each reporting unit. The valuation report should include documentation of supporting facts, key data and assumptions, and other considerations utilized in the analysis.

At Tall Oaks Partners, we bring an in-depth understanding of the valuation requirements of ASC 350. Our significant experience preparing valuation analyses for goodwill impairment purposes enables us to assist management in identifying areas of impairment risk, while preparing supportable valuation estimates that withstand the scrutiny of audit reviews. Have a question? Contact us at info@talloakspartners.com to get time scheduled with one of our Managing Partners.

1. Based on Financial Accounting Standards Board Accounting Standards Codification sections 350-20.