Statement of Financial Accounting Standards No. 72

FAS72 Status Page
FAS72 Summary

Accounting for Certain Acquisitions of Banking or Thrift Institutions

an amendment of APB Opinion No. 17, an interpretation of APB Opinions 16 and 17, and an amendment of FASB Interpretation No. 9

February 1983

Financial Accounting Standards Board
of the Financial Accounting Foundation
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FAS 72: Accounting for Certain Acquisitions of Banking or Thrift Institutions

an amendment of APB Opinion No. 17, an interpretation of APB Opinions 16 and 17, and an amendment of FASB Interpretation No. 9

FAS 72 Summary

This Statement amends APB Opinion No. 17, *Intangible Assets,* with regard to the amortization of the unidentifiable intangible asset (commonly referred to as goodwill) recognized in certain business combinations accounted for by the purchase method. If, and to the extent that, the fair value of liabilities assumed exceeds the fair value of identifiable assets acquired in the acquisition of a banking or thrift institution, the unidentifiable intangible asset recognized generally shall be amortized to expense by the interest method over a period no longer than the discount on the long-term interest-bearing assets acquired is to be recognized as interest income. This Statement also specifies that financial assistance granted to an enterprise by a regulatory authority in connection with a business combination shall be accounted for as part of the combination if receipt of the assistance is probable and the amount is reasonably estimable.

INTRODUCTION

1. The FASB has been asked to address the accounting for certain acquisitions of banking or thrift institutions. Those making the requests indicate that APB Opinions No. 16, *Business Combinations,* and No. 17, *Intangible Assets,* do not adequately address the conditions that have been present in some recent business combinations involving those institutions and that the use of the purchase method of accounting accompanied by the use of long amortization periods for purchased goodwill has produced postcombination operating results that are not reliable. Such combinations have recently become more frequent as a result of the economic climate, the move toward deregulation of certain financial institutions, and the involvement of financial institution regulators.

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SCOPE AND APPLICABILITY

2. This Statement applies to the acquisition of a commercial bank, a savings and loan association, a mutual savings bank, a credit union, other depository institutions having assets and liabilities of the same types as those institutions, and branches of such enterprises. Paragraphs 5 and 6 of this Statement apply to only those acquisitions in which the fair value of liabilities assumed by the acquiring enterprise exceeds the fair value of tangible and identifiable intangible assets acquired, and those provisions specify an amortization method for the portion of any unidentifiable intangible asset up to the amount of that excess. Opinion 17 and FASB Interpretation No. 9, *Applying APB Opinions No. 16 and 17 When a Savings and Loan Association or a Similar Institution Is Acquired in a Business Combination Accounted for by the Purchase Method,* also provide guidance as to the amortization of any additional unidentifiable intangible asset recognized in the acquisition. The provisions of paragraphs 4 and 7 apply to all acquisitions of banking and thrift institutions.

3. The provisions of paragraphs 8 through 11, which relate to the reporting of regulatory financial assistance, apply to all acquisitions of banking or thrift institutions. The Board understands that regulatory financial assistance agreements are not standardized and that the conditions under which assistance will be granted vary widely. As a result, this Statement does not specifically address all forms of regulatory financial assistance, but its provisions should serve as a general guide.

STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

Identified Intangible Assets

4. In a business combination accounted for by the purchase method involving the acquisition of a banking or thrift institution, intangible assets acquired that can be separately identified shall be assigned a portion of the total cost of the acquired enterprise if the fair values of those assets can be reliably [1] determined. The fair values of such assets that relate to depositor or borrower relationships [2] shall be based on the estimated benefits attributable to the relationships that *exist* at the date of acquisition without regard to new depositors or borrowers that may replace them. Those identified intangible assets shall be amortized over the estimated lives of those existing relationships.

Unidentifiable Intangible Asset

5. If, in such a combination, the fair value of liabilities assumed exceeds the fair value of

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tangible and identified intangible assets acquired, that excess constitutes an unidentifiable intangible asset. That asset shall be amortized to expense over a period no greater than the estimated remaining life of the long-term interest-bearing assets [3] acquired. Amortization shall be at a constant rate when applied to the carrying amount [4] of those interest-bearing assets that, based on their terms, are expected to be outstanding at the beginning of each subsequent period. The prepayment assumptions, if any, used to determine the fair value of the long-term interest-bearing assets acquired also shall be used in determining the amount of those assets expected to be outstanding. However, if the assets acquired in such a combination do not include a significant amount of long-term interest-bearing assets, the unidentifiable intangible asset shall be amortized over a period not exceeding the estimated average remaining life of the existing customer (deposit) base acquired. The periodic amounts of amortization shall be determined as of the acquisition date and shall not be subsequently adjusted except as provided by paragraphs 6 and 7 of this Statement. Notwithstanding the other provisions of this paragraph, the period of amortization shall not exceed 40 years.

6. Paragraph 31 of Opinion 17 specifies, among other things, that an enterprise should evaluate the periods of amortization of intangible assets continually to determine whether later events and circumstances warrant revised estimates of useful lives. In no event, however, shall the useful life of the unidentifiable intangible asset described in paragraph 5 of this Statement be revised upward.

7. For purposes of applying paragraph 32 of Opinion 17,[5] if a large segment or separable group of the operating assets of an acquired banking or thrift institution, such as branches, is sold or liquidated, the portion of the unidentifiable intangible asset attributable to that segment or separable group shall be included in the cost of the assets sold. If a large segment or separable group of the interest-bearing assets of an acquired institution is sold or liquidated and if the benefits attributable to the unidentifiable intangible asset have been significantly reduced,[6] that reduction shall be recognized as a charge to income.

Regulatory-Assisted Combinations

8. In connection with a business combination, a regulatory authority may agree to pay amounts by which future interest received or receivable on the interest-bearing assets acquired is less than the interest cost of carrying those assets for a period by a stated margin. In such a case, the projected assistance, computed as of the date of acquisition based on the interest-rate margin existing at that date, shall be considered as additional interest on the interest-bearing assets acquired in determining their fair values for purposes of applying the purchase method (paragraphs 87 and 88 of Opinion 16). The carrying amount of those interest-bearing assets shall not be adjusted for subsequent changes in the estimated amount of assistance to be received. Actual assistance shall be reported in income of the period in which it accrues. Notwithstanding the above provisions, if an enterprise intends to sell all or a portion of the interest-bearing assets acquired, those assets shall not be stated at amounts in excess of their current market values.

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9. Other forms of financial assistance may be granted to a combining enterprise or the combined enterprise by a regulatory authority in connection with a business combination accounted for by the purchase method. If receipt of the assistance is probable and the amount is reasonably estimable, that portion of the cost of the acquired enterprise shall be assigned to such assistance. Assets and liabilities that have been or will be transferred to or assumed by a regulatory authority shall not be recognized in the acquisition. If receipt of the assistance is not probable or the amount is not reasonably estimable, any assistance subsequently recognized in the financial statements shall be reported as a reduction of the unidentifiable intangible asset, described in paragraph 5, that was recognized in the acquisition. Subsequent amortization shall be adjusted proportionally. Assistance recognized in excess of that intangible asset shall be reported in income.

10. Under certain forms of assistance granted in connection with a business combination, the combined enterprise may agree to repay all or a portion of the assistance if certain criteria related to the level of future revenues, expenses, or profits are met. Such a repayment obligation shall be recognized as a liability and as a charge to income at the time the conditions in paragraph 8 of FASB Statement No. 5, *Accounting for Contingencies,* are met. This paragraph does not address repayments of assistance granted in exchange for debt or equity instruments.

Disclosures

11. The nature and amounts of any regulatory financial assistance granted to or recognized by an enterprise during a period in connection with the acquisition of a banking or thrift institution shall be disclosed.

Amendments to Other Pronouncements

12. The following footnote is added to the end of (a) paragraph 29 of Opinion 17, (b) the first sentence of paragraph 30 of Opinion 17, (c) the second sentence of paragraph 31 of Opinion 17, and (d) paragraph 9 of Interpretation 9:

> *Paragraphs 5 and 6 of FASB Statement No. 72, *Accounting for Certain Acquisitions of Banking or Thrift Institutions,* specify an exception to the provisions of this [Opinion/Interpretation] with respect to the amortization of goodwill recognized in certain acquisitions of banking or thrift institutions.

13. The second sentence of paragraph 8 of Interpretation 9 is amended to insert the word *reliably* and the related footnote as follows:

> If the amount paid for any such factor can be reliably* determined, that amount shall not be included in goodwill.

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*Reliability embodies the characteristics of representational faithfulness and verifiability, as discussed in FASB Concepts Statement No. 2, *Qualitative Characteristics of Accounting Information.*

14. The following sentence is added to the end of paragraph 8 of Interpretation 9:

> The fair values of identified intangible assets that relate to depositor or borrower relationships (refer to paragraphs 8(a) and 8(b)) shall be based on the estimated benefits attributable to the relationships that exist at the date of acquisition without regard to new depositors or borrowers that may replace them. Those identified intangible assets shall be amortized over the estimated lives of those existing relationships.

Effective Date and Transition

15. This Statement shall be applied prospectively to business combinations initiated [7] after September 30, 1982 with earlier application encouraged. Retroactive application to a business combination initiated prior to October 1, 1982 is permitted but not required. If, prior to March 1, 1983, an enterprise has issued financial statements in which the provisions of this Statement have not been applied to a business combination initiated and consummated after September 30, 1982, those financial statements shall be restated when they are first presented with financial statements for subsequent periods, or the opening balance of retained earnings for that subsequent period shall be appropriately adjusted if they are omitted. In addition, the financial statements shall, in the year the standards are first applied, disclose the nature of any restatement and its effect on income before extraordinary items, net income, and related per-share amounts for each restated year presented.

The provisions of this Statement need not be applied to immaterial items.

This Statement was adopted by the unanimous vote of the seven members of the Financial Accounting Standards Board:

Donald J. Kirk, *Chairman*
Frank E. Block
Victor H. Brown
John W. March
David Mosso
Robert T. Sprouse
Ralph E. Walters

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Appendix A: BACKGROUND INFORMATION

16. Business combinations involving banking or thrift institutions have become frequent. Such combinations have increased, in part, as a result of the relaxed restrictions on interstate banking, the involvement of financial institution regulators, and the current trend toward deregulation of those industries. Various accounting and reporting questions have been raised as a result of those combinations.

17. Banking and thrift institutions, whose primary assets and liabilities are interest-bearing instruments, generally are regulated under laws of the various states or the federal government, or both. The qualified deposits of most banking and thrift institutions are insured by regulatory agencies, and as a result, those institutions are subject to the rules and regulations of those agencies. Because of its position as an insurer, a regulatory agency may provide financial assistance to an institution to minimize the agency's risk of loss.

18. Current economic and competitive conditions have adversely affected the financial position and operations of many financial institutions, particularly savings and loan associations and mutual savings banks. In particular, continued high interest rates have eroded interest margins, and competitive pressures in some cases have resulted in depositors' transferring funds to other kinds of enterprises. Many savings and loan associations and mutual savings banks have reported net losses during recent periods and some have failed to meet the minimum net worth requirements established by regulatory agencies. Failure to meet those requirements may result in a regulator's arranging or encouraging a merger with another enterprise. In some cases, a regulatory authority such as the Federal Deposit Insurance Corporation, the Federal Savings and Loan Insurance Corporation, the National Credit Union Share Insurance Fund, or a state insurance fund may grant financial assistance to an enterprise as an inducement for that enterprise to assume the assets, liabilities, and operations of a banking or thrift institution that has failed, or is about to fail, those minimum regulatory net worth requirements.

19. A majority of the recent business combinations referred to above were mergers of mutual thrift institutions. Most thrifts are mutual institutions, that is, they are owned by their depositors, rather than by stockholders. The combination of two mutual thrifts generally is effected without any payment of cash or other assets by either institution to the previously separate ownership interests. Instead, one institution absorbs the operations of the other institution, thereby obtaining the assets and assuming the liabilities of that institution. Prior to 1981, substantially all mergers of mutual thrifts were accounted for using the pooling-of-interests method described in Opinion 16. Recently, however, the majority of such mergers have been accounted for using the purchase method of accounting.

20. Opinion 16 and Interpretation 9 specify how an acquiring enterprise should allocate the

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cost of an acquired enterprise to the assets acquired and the liabilities assumed in applying the purchase method. Paragraph 88 of Opinion 16 indicates that, as a general guide, a portion of the cost should be assigned to intangible assets that can be identified and named based on appraised values. Paragraph 87 of that Opinion indicates that the cost of the acquired enterprise in excess of the sum of the amounts assigned to identifiable assets acquired less liabilities assumed should be reported as goodwill, which is an unidentifiable intangible asset. Opinion 17 and Interpretation 9 also apply to intangible assets acquired in business combinations accounted for by the purchase method.

21. Opinion 17 specifies that any intangible asset should be amortized by systematic charges to income over the period to be benefited, but that period may not exceed 40 years. That Opinion sets forth factors that should be considered in estimating the useful lives of intangible assets. Paragraph 27(c) of that Opinion specifies that the "effects of obsolescence, demand, competition, and other economic factors may reduce a useful life."

22. When banking or thrift institutions are acquired in periods of high interest rates, application of the purchase method and subsequent amortization of acquired intangibles over an extended period of time may produce a significant effect on the subsequent reported results of operations of the combined enterprise. In such periods, if low-rate interest-bearing assets are discounted to their fair values using current interest rates, the fair value of liabilities assumed may exceed by a substantial amount the fair value of tangible and identifiable intangible assets acquired. That excess often has been reported as goodwill in applying the purchase method under Opinion 16. The discount on the interest-bearing assets is amortized to income over the remaining lives of those assets using the interest method. If the goodwill is amortized straight-line over a period that exceeds the period the discount is amortized to income, the subsequent reported earnings for the combined enterprise may show a dramatic increase compared with the sum of the separate results of those enterprises absent the combination.

23. Some believe that the goodwill recognized in such circumstances generally does not represent a negotiated premium paid for intangible factors that are expected to enhance future profit levels. They contend that the amount recognized is often merely a function of current interest rates. Others believe that the current economic and competitive conditions facing the banking and thrift industries do not support the selection of a 40-year estimated useful life, especially in view of the anomalous effect on postcombination earnings that the use of such an extended life can produce. Still others believe that goodwill recognized in the acquisition of such institutions is not different in nature from goodwill recognized in other acquisitions and that the existing provisions of Opinion 17 provide adequate guidance in determining the estimated life.

24. In July 1982, the Accounting Standards Executive Committee of the AICPA requested the FASB to address the accounting for business combinations of mutual thrift institutions. The committee requested the Board to issue guidance that would produce meaningful results in accounting for these combinations and reduce the diversity in practice. On August 11, 1982, the

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Board added to its agenda a project to address the amortization of the unidentifiable intangible asset recognized in certain acquisitions of banking or thrift institutions. On October 7, 1982, the Board issued an FASB Exposure Draft, *Accounting for Certain Acquisitions of Banking or Thrift Institutions*. The Board received 80 letters of comment on that Exposure Draft. On December 13, 1982, the Board conducted a public hearing on the Exposure Draft. Thirteen organizations and individuals presented their views at the hearing.

Appendix B: BASIS FOR CONCLUSIONS

25. This appendix discusses the significant comments received on the Exposure Draft and the factors deemed significant by the Board in reaching the conclusions in this Statement, including alternatives considered and reasons for accepting some and rejecting others. Individual Board members gave greater weight to some factors than to others.

Scope

26. Many respondents to the Exposure Draft pointed out that the issues of purchase accounting and the recognition and amortization of intangible assets are not unique to acquisitions of banking and thrift institutions. They suggested that if the Board perceives a problem with respect to those issues, it should undertake a comprehensive project to readdress the accounting for business combinations by all types of enterprises. They stated that the Exposure Draft discriminated against thrift institutions in particular and that such an approach ran counter to the Board's general practice of promulgating standards that are evenhanded and applicable to all enterprises.

27. Board members agree that questions concerning purchase accounting and the recognition and amortization of intangible assets are not unique to acquisitions of banking and thrift institutions but believe that a comprehensive reconsideration of Opinions 16 and 17 should not be undertaken at this time. Accounting for business combinations and intangible assets are subjects with a long history of diverse views and controversy among standard setters and among others interested in financial reporting—preparers, users, auditors, academics, and the financial press. As one would expect, individual Board members have different views on those subjects, and it is neither feasible nor appropriate to reconsider the pervasive issues of business combinations and intangible assets in the context of this narrow, but significant and urgent, practice problem. Accordingly, the Board decided to restrict the scope of this Statement to certain combinations involving the acquisition of a banking or thrift institution in order to address that problem in a timely manner. However, most Board members believe that if goodwill is recognized in the acquisition of any enterprise having liabilities in excess of its assets it generally would be short lived.

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Unidentifiable Intangible Asset

28. Many respondents stated that the Board's proposal to equate the amortization period for an unidentifiable intangible asset with the average life of the interest-bearing assets acquired is arbitrary and conceptually unsound, and they urged the Board to abandon the project. They stated that enterprises that acquire banking and thrift institutions pay a premium to gain entry into new markets, to acquire established branches with existing customer relationships, to acquire an existing deposit base, and for other factors. They also indicated that goodwill recognized in a banking or thrift acquisition relates to the expectation of enhanced future earnings just as it does in acquisitions of other types of enterprises. They pointed out that the proposed amortization method implies that an acquiring enterprise has paid a premium to acquire an institution's interest-bearing assets, when in fact that aspect of the acquisition is of least importance. Most of those respondents stated that the existing guidance in Opinion 17 is sufficient to allow enterprises and auditors to reach reasonable conclusions about the useful life of the unidentifiable intangible.

29. All Board members recognize that acquisitions of banking and thrift institutions seldom, if ever, are consummated for the purpose of acquiring a portfolio of interest-bearing assets. In both Interpretation 9 and this Statement, the Board has emphasized that intangible factors of the nature referred to in the preceding paragraph should be identified and recognized if their fair values can be reliably measured. The Board understands that identified intangibles have not always been separately recognized in the past.

30. The Board believes that the use of a 40-year maximum amortization period in the face of existing economic and competitive uncertainties confronting the banking and thrift industries is inappropriate. That accounting for such combinations produces results that lack economic substance, that destroy both consistency of reporting by the enterprise and comparability among similar enterprises, and that have the capacity to mislead users and damage the credibility of financial reporting. Accordingly, the Board concluded that more explicit guidance was needed to improve the relevance and reliability of financial reporting.

31. For a variety of reasons discussed below, the Board believes that if the fair value of the liabilities assumed in an acquisition exceeds the fair value of tangible and identified intangible assets acquired, the remaining life of the long-term interest-bearing assets acquired is an appropriate maximum period for amortizing the unidentifiable intangible asset attributable to that excess. It is important to observe that Board members support this industry-specific standard primarily because they agree that a rapid and pragmatic resolution of the problem is essential.

32. Most Board members believe that Opinion 16 requires that the amount by which the fair value of liabilities assumed exceeds the fair value of identifiable assets acquired be recognized as an unidentifiable intangible asset. They also believe that this excess should be amortized over a

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relatively short period because of the uncertainty about the nature and extent of the estimated future benefits related to that asset. Ordinarily, the form of consideration given in a business combination (for example, cash, assumption of debt, or issuance of stock) does not affect the reporting of the transaction. However, the Board believes that a deficiency of identifiable assets (determined using fair values) is indicative of uncertainty as to the recoverability of any unidentifiable intangible and augments the uncertainty inherent in the economic and competitive environment of banking and thrift institutions. In many cases, the acquired banking or thrift institution has incurred recent operating losses, and its prospects for returning (or contributing) to profitable operations in the future depend in large part on the level of future interest rates. The nature and extent of future benefits related to the intangible asset also may be impacted by the possible deregulation of the banking and thrift industries.

33. Most Board members also support the amortization method specified in paragraph 5 as a practical solution for eliminating what they believe is an unwarranted positive effect on earnings when a troubled financial institution is acquired and an unidentifiable intangible asset is recognized and amortized over an extended period. They agree that an increase in earnings may occur after a business combination as a result of acquiring a profitable enterprise or because of economic advantages that the combination has produced, but they believe that reporting a substantial increase in earnings without any substantive change in the economic condition of the combined enterprise is not representationally faithful and that the frequency of such reporting has harmed the credibility of financial reporting in general. Some Board members also support an amortization method based on the lives of the interest-bearing assets acquired because they believe that that period more closely approximates the useful life of a customer list or deposit base than does a 40-year period.

34. Some Board members also believe that the purchase method of accounting may be inappropriate for most combinations of *mutual* banking and thrift institutions and note that a majority of thrift institutions are organized under that form of ownership. Combinations of those institutions generally do not involve the transfer of cash, other assets, or equity interests to the previous owners of the acquired institution. Those Board members further support the amortization method specified in paragraph 5 because it often results in reporting approximately the same amount of postcombination net income that would have been reported if the combination had been accounted for by combining the previous carrying amounts of the two enterprises.

Nature of Problem

35. Several respondents said the Board should reexamine the applicability of Opinion 16 to a combination of mutual banking or thrift institutions instead of pursuing the tentative conclusions in the Exposure Draft. They stated that Opinion 16's criteria for using the pooling-of-interests method are difficult to apply in a combination of mutuals and indicated that those criteria were not designed with mutual institutions in mind. Some of those respondents recommended that the Board explain how the pooling-of-interests criteria should be applied in a combination of

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mutuals. Others stated that the Board should mandate the use of the pooling-of-interests method in such combinations. Still others indicated that purchase accounting should be used.

36. Board members considered addressing the question of whether the methods of accounting for a business combination specified in Opinion 16 (that is, the purchase method and the pooling-of-interests method) are appropriate for business combinations of mutual banking and thrift institutions. Most Board members believe that (a) the Accounting Principles Board in Opinion 16 did not specifically consider such combinations and (b) application of the criteria in paragraphs 46-48 of Opinion 16 to combinations of mutual institutions is not clear. Most Board members believe such a reconsideration would be time-consuming and would delay resolution of the pressing accounting question at hand. The Board also notes that the reporting problem being addressed is not limited to combinations of mutuals. Stockholder-owned banking and thrift institutions are also involved in business combinations. The Board concluded that a broad consideration of accounting for business combinations of mutuals should be included as part of any future project to readdress accounting for business combinations in general.

37. Some respondents stated that the reporting problems addressed in this project have resulted from the failure of enterprises and auditors to properly apply the existing guidance in Opinion 17. Some of those respondents said that a 40-year life for goodwill may not be appropriate in many circumstances but suggested that the Board view the current problem as an auditing or enforcement matter and not take on the role of a mediator. They believe that the existing principles of Opinion 17 are sound and should not be changed to address such a limited problem. Some of those respondents provided the Board with data indicating the problem was not as widespread as some others had asserted. However, research by the FASB staff indicated that the use of a 40-year life for goodwill has become common. The Board assessed both the severity of the problem and the adequacy of existing guidance and concluded that, on balance, more explicit guidance was needed to minimize diversity in practice and to improve the relevance and reliability of financial reporting.

Perceived Economic Consequences

38. Some respondents recommended that the Board withdraw the proposal because its adoption would have adverse economic consequences. Those respondents stated that the adoption of the provisions of the Exposure Draft in a final Statement would (a) prevent economically sound mergers from occurring, (b) put a strain on the resources of regulatory insurance agencies because potential acquiring enterprises would demand an increased amount of financial assistance, (c) frustrate the thrift industry's survival plans, or (d) impair an enterprise's ability to restructure and meet changing economic conditions. The Board was not persuaded by those arguments. The Board believes that this Statement will not affect an enterprise's ability to survive or restructure. Those abilities are a function of future cash flows, management action, and legal and regulatory restrictions rather than a function of accounting standards. In addition, the Board believes that the amortization provisions of this Statement will produce accounting information that is more relevant, reliable, and neutral for purposes of

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decision making. A primary focus of financial reporting is information about an enterprise's performance provided by measures of earnings and its components. The need for relevant and reliable measures of earnings following the acquisition of a banking or thrift institution was a major factor contributing to the Board's decision.

Subsequent Dispositions of Interest-Bearing Assets

39. Many respondents asked whether the proposed amortization method and the provision of paragraph 11(b) of the Exposure Draft were intended to require an enterprise to reduce goodwill proportionally when all or a portion of the acquired interest-bearing assets are sold subsequent to the acquisition date. Some of those respondents stated that such reporting may be appropriate, but only if the acquiring enterprise sells or liquidates a large segment or separable group of those assets (paragraph 32 of Opinion 17). They requested the Board to clarify the meaning of *large segment or separable group of assets* in the context of the banking and thrift industries. Other respondents also asked for clarification and stated that paragraph 32 of Opinion 17 should not apply in *any* subsequent sale of acquired interest-bearing assets, such as mortgage loans and investment securities. They pointed out that some banking and thrift institutions sell and reinvest in interest-bearing assets every day and that the benefits attributable to goodwill are unaffected by the presence or absence of such fungible assets. The Board generally agreed with that latter view, and this Statement specifies that the sale of all or a portion of acquired interest-bearing assets does not automatically require a reduction in goodwill. A determination of whether a reduction in goodwill is appropriate should be based on the individual facts and circumstances. For example, if a sale of a large group of interest-bearing assets is accompanied by the loss of a significant and valuable customer base, a reduction in goodwill likely would be appropriate. On the other hand, if the proceeds of sale are reinvested in other forms of interest-bearing or other assets, no such reduction is necessary if there has been no reduction in the benefits attributable to goodwill.

Identified Intangibles

40. Several respondents stated that the adoption of a shorter useful life for goodwill recognized in certain acquisitions of banking or thrift institutions would induce affected enterprises to assign a greater portion (or all) of the excess purchase price to identified intangibles rather than to goodwill. Some of those respondents said that amounts often have not been assigned in the past to identified intangibles because (a) appraised values were not readily determinable, (b) those intangible factors often have indefinite lives, and (c) factors such as core deposits, branch networks, and territorial advantages represent the essence of goodwill. They questioned whether the benefits of separate identification would justify the costs. Other respondents said the Board should clarify Opinion 16 and Interpretation 9 to indicate that the measurements of such identified intangibles must be representationally faithful and verifiable. They stated that, without such guidance, unreliable amounts may be assigned to identified intangibles, thus circumventing this Statement's intent.

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41. The Board reaffirms the principles in Opinion 16 and Interpretation 9 that require identified intangibles to be recognized apart from goodwill and amortized over their estimated useful lives. The Board does not view as undesirable any increased effort to identify and measure specific intangible assets acquired in a business combination. However, the Board agrees with those respondents who stated that such intangible assets should be recognized only when they can be separately identified and their fair values can be reliably measured. Accordingly, this Statement specifies that the measurements of identified intangible assets must be verifiable and representationally faithful. The Board disagrees with those respondents who stated that intangible assets attributed to deposit accounts and customer relationships generally have indefinite lives. Those respondents viewed such relationships as being constantly renewed and growing and, therefore, indicated that a 40-year useful life may often be appropriate. The Board notes that Interpretation 9 refers to intangible factors representing the capacity of *existing* accounts to generate future income or new business. The Board recognizes that many enterprises purchase a banking or thrift institution with the expectation of maintaining and even expanding the existing customer base and, thereby, the value of the related intangible asset; however, only purchased intangible assets are capitalizable under present generally accepted accounting principles. The Board believes that the cost and useful life of acquired intangible assets should not reflect the costs and expectations of developing, maintaining, or restoring such intangibles after they are acquired.

Other Matters

42. A few respondents requested the Board to explain how the provisions of the Exposure Draft should be applied when a combination does not involve the acquisition of a significant amount of interest-bearing assets, such as in the acquisition of a branch location. The Board understands that such acquisitions often involve the assumption of deposit liabilities by the acquiring enterprise in exchange for a cash payment in an amount less than the fair value of the deposit liabilities assumed. In such circumstances, the Board believes identifiable intangible assets should be recognized as provided in Opinion 16, Interpretation 9, and paragraph 4 of this Statement. If a portion of the purchase price is allocated to an unidentifiable intangible, the Board believes that amount should be amortized over a relatively short period of time, not to exceed the estimated average remaining life of the existing customer base acquired. The value of a customer base was cited most often by respondents as the primary factor acquired in such transactions.

43. Some respondents questioned portions of the Exposure Draft that dealt with reporting regulatory financial assistance granted to an enterprise as an inducement for that enterprise to acquire a banking or thrift institution. Some stated that subsequent repayments of regulatory assistance should not be charged to income automatically because such reporting may not be consistent with the initial reporting of the assistance. The Board understands that repayment requirements generally are related to future profitability levels or other criteria based on future revenues or expenses. In those cases, the Board believes the nature of the repayment is similar to a profit-sharing arrangement and that the repayments should be charged to expense, regardless

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of the manner in which the assistance was initially reported.

44. A few respondents stated that estimates of regulatory reimbursements for any future operating losses should not be recognized at the time of combination because the amount of assistance cannot be reliably measured. The Board is in general agreement with those respondents. However, the Board believes that certain forms of regulatory assistance expected to be effective in indemnifying an enterprise from all or a portion of any losses that may result from holding certain low-rate interest-bearing assets acquired in a combination accounted for using the purchase method should be taken into consideration in determining the fair value of the assets acquired. Those forms of assistance represent probable future economic benefits that will result in future cash flows as a result of either (a) payment by a regulatory authority (if interest rates increase or remain constant) or (b) reduced cost of funds (if interest rates decline). The Board believes that reporting the effect of this benefit as part of the carrying amount of the interest-bearing assets acquired is a reasonable approach.

45. A few respondents suggested that this Statement should be effective for business combinations initiated after the issuance of the Statement rather than for combinations initiated after September 30, 1982. They argued that it is inappropriate to establish a retroactive effective date in a Statement that changes existing standards, especially when those standards have previously been acceptable. Although the Board hopes that the conditions that led to the reporting problems addressed by this Statement are temporary, the accounting for intangible assets may affect financial reporting for an extended period. The Board considered when this Statement should become effective and the transition method that should be applied by enterprises in adopting it in that light, weighing considerations of consistent, comparable, and credible reporting with fairness to preparers who have adopted or may yet adopt practices this Statement would change, fairness to those who did not, and fairness to users of financial reports. Those are subjective considerations and individual Board members attached differing weights. Accordingly, the effective date of September 30, 1982 and the prospective application reflect a compromise among Board members, some of whom would prefer an earlier effective date or retroactive application or both, and others who would prefer that the Statement become effective upon issuance.

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Footnotes

FAS72, Footnote 1--Reliability embodies the characteristics of representational faithfulness and verifiability, as discussed in FASB Concepts Statement No. 2, *Qualitative Characteristics of Accounting Information.*

FAS72, Footnote 2--Examples of intangible assets related to depositor or borrower relationships are described in paragraphs 8(a) and 8(b) of Interpretation 9.

FAS72, Footnote 3--For purposes of this Statement, long-term interest-bearing assets are interest-bearing assets with a remaining term to maturity of more than one year.

FAS72, Footnote 4--*Carrying amount* is the face amount of the interest-bearing asset plus (or minus) the unamortized premium (or discount).

FAS72, Footnote 5--Paragraph 32 of Opinion 17 states: "a large segment or separable group of assets of an acquired company or the entire acquired company may be sold or otherwise liquidated, and all or a portion of the unamortized cost of the goodwill recognized in the acquisition should be included in the cost of the assets sold."

FAS72, Footnote 6--For example, if a sale of a large group of interest-bearing assets is accompanied by the loss of a significant and valuable customer base, a reduction in goodwill likely would be appropriate. On the other hand, if the proceeds of sale are reinvested in other forms of interest-bearing or other assets, no such reduction may be necessary.

FAS72, Footnote 7--Refer to Opinion 16, paragraph 46(a) and footnote 14 to paragraph 97. Planned combinations involving a banking or thrift institution may be subject to approval by a regulatory authority and to a final determination concerning the amount of regulatory financial assistance to be granted. Under those circumstances, a combination shall be considered initiated if an announcement or notification as required by paragraph 46(a) of Opinion 16 has been made. A plan of combination involving only mutual banking or thrift institutions often is communicated by an enterprise to the board of directors of an institution rather than to the owners of the institution. In those circumstances, notification to a board of directors constitutes notification to shareholders for purposes of determining the date a business combination is initiated.

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