

Toward Business Literacy: Accounting Outlines



Goodwill and R&D

Goodwill

- When in a business combination, if purchase price is greater than the fair market value of net tangible and identifiable intangibles, the difference is goodwill.
 - Associated with the total company only on purchase
 - No such thing as internally-generated goodwill
 - Reevaluate liabilities at present value if rates change
 - Change estimates and reevaluate replacement cost for assets
- Why goodwill?
 - Established reputation, good credit rating, top management team, well-trained employees, future earning potential & asset structure
- When do we write off goodwill?
 - Goodwill has an indefinite life and should be reevaluated periodically and charged to income statement if impaired
 - Impairment is when future cash flows (undiscounted) plus the disposition cost is less than carrying value
- Negative goodwill
 - When the fair value of assets exceeds the purchase price
 - Excess allocated pro-rata to non-financial assets
 - Remaining excess is an extraordinary gain

Research and Development

- Always expensed when incurred
- Research: planned search or critical investigation aimed at discovery
- Development: translate research findings or knowledge into a plan or design for new or improved product or process.
- Materials, equipment & facilities: expensed unless useful for alternate purpose
- Personnel: salaries and wages are expensed
- Purchased intangibles: expensed (or capitalized if other uses)
- Contract services from others: expensed
- Indirect costs must be related
- Similar to R&D
 - Start-up costs: organization, legal, accounting- expensed
 - Initial operating losses: FASB 7 gives no special treatment to new companies—losses have no future service potential
 - Advertising costs: expensed as incurred or when advertising shows
 - Computer software is special
 - R&D is expensed until → technological feasibility
 - After feasibility → costs capitalized and amortized
 - Greater of current revenues to current and anticipated