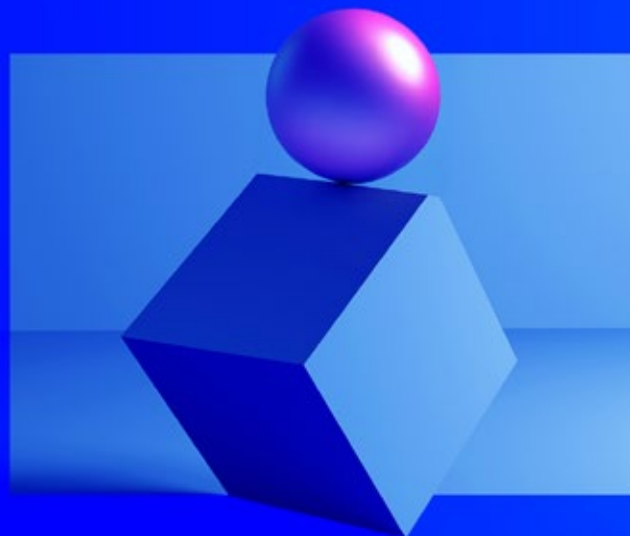




Goodwill impairment testing—practical valuation FAQs in uncertain markets

A technical advisory with concise answers on uncertainty, market participant acquisition premiums, market-cap reconciliation, and subsequent events



This document is designed to assist finance leaders, valuation specialists, and auditors navigate the most judgment-intensive areas of goodwill impairment testing during volatile markets—so conclusions are supportable, measurement-date appropriate, and clearly documented.



Understand practical ways to reflect uncertainty in fair value measurements (cash-flow scenarios versus discount-rate adjustments) and what documentation typically needs to accompany those judgments.



Apply a structured approach to supporting market participant acquisition premiums (MPAPs, sometimes referred to as control premiums) when transaction data is stale or markets are repricing risk, including when incremental quantitative support is expected.



Use market capitalization thoughtfully (including averaging considerations and subsequent-event boundaries) when reconciling reporting unit conclusions to observable market evidence.

This document consolidates common technical questions that arise when goodwill impairment testing occurs during heightened volatility and economic uncertainty. The answers are intended to support a measurement-date fair value conclusion under US generally accepted accounting principles (GAAP) and should be considered in light of a subject company's facts and circumstances.

FAQ 1: How can uncertainty be incorporated into the valuation analysis?

At the onset of a stock market downturn—or when the stock market is strong but uncertainty prevails over the economy, policy, technology, or other external factors—capturing uncertainty in a valuation may require widening ranges and recalibrating key inputs (e.g., discount rates and market multiples). Where appropriate, scenario-based or probability-weighted cash flows can help reflect uncertainty in projections; alternatively, if reflecting the effect in cash flows is

not feasible, then a well-supported adjustment to the discount rate may be warranted.

Regardless of the selected approach, robust contemporaneous documentation is typically required to distinguish short-term volatility from structural repricing and to support market participant assumptions. Sensitivity analyses and ranges of outcomes can be useful to assess and document the effect of uncertainty on fair value.

FAQ 2: How should the market participant acquisition premium be estimated when observable M&A transactions pre-date a market decline?

In goodwill impairment tests, MPAP can be a critical assumption requiring significant support and may be expressed as a percentage of business enterprise value (BEV) or market capitalization. As market conditions change, it can become difficult to reconcile market capitalization under a “normal” MPAP, making it important to reassess what range of premiums is supportable based on market participant evidence at the measurement date.

MPAPs generally require quantitative support, particularly as the premium increases and deviates from market averages. Transaction benchmarks may be informative, but additional quantitative support (including identifying and quantifying market participant synergies) is typically expected when

premiums approach the upper end of an accepted range. Historical observations can inform judgment, but they should not be treated as a substitute for current, company-specific support.

It is important to consider how MPAPs may be influenced by economic cycles. In the following tables, we compare observable MPAPs for the last two significant economic downturns and periods of increased economic uncertainty.

As shown in the table below, when comparing the period of the financial crisis to a stable period before (2006–2007) the crisis, we observed MPAPs that were noticeably elevated during the crisis.

Observed BEV MPAP increases during the financial crisis

Percentile	2006–2007	2008–2009	Difference
25.0%	8.3%	7.9%	-0.4%
50.0%	20.2%	30.3%	10.1%
75.0%	36.8%	59.9%	23.1%

Source: KPMG analysis based on information provided by S&P Capital IQ

A similar observation can be made for implied MPAPs during the COVID-19 pandemic as detailed in the following table. It should be noted that the

implied increase in the MPAP was less pronounced during this period compared to the financial crisis. Nevertheless, the effect was still observable.

Observed BEV MPAP increases during COVID-19

Percentile	2018–2019	2020–2021	Difference
25.0%	6.6%	8.9%	2.2%
50.0%	18.3%	24.6%	6.2%
75.0%	37.2%	43.2%	6.0%

Source: KPMG analysis based on information provided by S&P Capital IQ

While it may be more common to see higher premiums in these periods, it is critical to appropriately support these assumptions with sufficient market data. In general, as the MPAP

increases and deviates from market averages, more robust support will be required. The Securities and Exchange Commission (SEC) staff made the following observations:

“I would also note that the amount of supporting evidence supporting your judgment would likely be expected to increase as any control premium increases.”

— SEC Deputy Chief Accountant Robert G. Fox III, Remarks before the 2008 AICPA National Conference on Current SEC and PCAOB Developments¹

As MPAP increases, transaction comparability should be reviewed in detail, and additional quantitative analyses are generally expected when MPAP significantly influences an impairment conclusion or is at the upper end of an observed industry range. One common approach is to quantify the present value of market participant synergies (e.g., identifying corporate costs that a market participant acquirer could eliminate or leverage) and document the assumptions used.

In these cases, a detailed analysis of the qualitative factors referenced in the Appraisal Foundation’s *Valuations in Financial Reporting Valuation Advisory 3: The Measurement and Application of Market Participant Acquisition Premiums* can be helpful.

Note: Historical data and observations are intended for reference only. Goodwill impairment testing and related valuation analyses must be based on current market participant assumptions and reflect the subject company’s specific facts and circumstances at the measurement date, in accordance with US GAAP.



FAQ 3: Does a company need to reconcile reporting unit fair values to market capitalization when some, but not all, reporting units are tested?

Generally, yes, although the approach may differ. One approach is to consider the current fair value of the quantitatively tested reporting units plus an evidence-based estimate of the current fair value for remaining reporting units, typically adjusted from the

most recent quantitative measurements to reflect the current economic environment. Another approach is to perform a high-level market multiple analysis for reporting units that are not otherwise quantified at the measurement date.

¹ <https://www.sec.gov/news/speech/2008/spch120808rgf.htm>

FAQ 4: Can a company use an average stock price when reconciling to market capitalization?

Generally, yes. In volatile market conditions, it may be appropriate in certain circumstances to consider market capitalization based on an average share price over a reasonable period as a better estimate of fair value; however, it would not be reasonable to

ignore recent declines in stock price if those declines indicate more than temporary repricing of risk or reduced market expectations of future cash flows. The following SEC staff guidance continues to be cited in practice in periods of economic uncertainty.

“When a registrant is evaluating an appropriate control premium, I believe that an important factor to consider is their recent trends in market capitalization. Note that I said recent trends in their market capitalization. Especially in volatile markets, and other unique circumstances, it may not always be reasonable to look at a single day’s market capitalization. In some cases, I believe it would be more reasonable to look at market capitalization over a reasonable period of time leading up to the date at which you are testing for potential impairment. However, I would also note that it would not be reasonable for a registrant to simply ignore recent declines in their stock price, as the declines are likely indicative of factors the registrant should consider in their determination of fair value...”

—SEC Deputy Chief Accountant Robert G. Fox III, Remarks before the 2008 AICPA National Conference on Current SEC and PCAOB Developments²

In sudden volatility and rapid declines, selecting a “reasonable” averaging period requires judgment and should precede (and not extend beyond) the measurement date. Averaging is intended to smooth day-to-day volatility and should not be used to mask a fundamental shift in the underlying economic trajectory; documentation should articulate why price movements in the window reflect volatility rather than a new baseline. When markets react to specific events that fundamentally change the perception of the economy and how market participants perceive the world, it would generally not be appropriate for a company to use an average that includes dates before that specific event. A distinction should be

considered between short-term volatility and a fundamental, potentially permanent, repricing of the company’s equity.

The length of the averaging period will also depend on company-specific facts and circumstances. For example, it may not be appropriate to consider prices in periods before certain entity-specific events (e.g., loss of key customers, revision(s) in earnings guidance, or reductions in force) as the change in price may be related to factors other than volatility. In any case, we would expect a company to prepare robust documentation of its key judgments in determining the averaging period.

FAQ 5: Can a company use market prices after the reporting date in its average market price?

Generally, no. Changes in market prices after the reporting date typically do not reflect conditions at the reporting date and are generally nonrecognized

subsequent events, though they may warrant reevaluating whether all conditions existing at the reporting date were appropriately considered.

² <https://www.sec.gov/news/speech/2008/spch120808rgf.htm>

How to use this series

This technical advisory provides practical valuation FAQs for uncertain markets; see the first document of this series, [*Goodwill impairment in volatile markets—what changes \(and what doesn't\)*](#), for market context and the final document of the series, [*Goodwill impairment—triggering events and process guide*](#), for a triggering-events and process workflow.

Additional resources

- [KPMG Handbook: Accounting for economic disruption](#) (chapters 5 and 6)
- [KPMG Handbook: Impairment of nonfinancial assets](#)
- [Appraisal Foundation: Valuations in Financial Reporting Valuation Advisory 3—The Measurement and Application of Market Participant Acquisition Premiums](#)
- [AICPA: Accounting and Valuation Guide—Testing Goodwill for Impairment](#)

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