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To the Point

FASB – final guidance

FASB issues guidance on accounting for government grants by business entities

The standard is similar to the guidance in IAS 20 that many business entities already apply by analogy to account for government grants.

What you need to know

- The FASB issued final guidance on the recognition, measurement and presentation of a government grant received by a business entity to reduce diversity in practice.
- The Board leveraged the guidance in IAS 20 on accounting for government grants, with certain targeted improvements, to develop the ASU.
- For public business entities, the guidance is effective for fiscal years beginning after 15 December 2028 and interim periods within those fiscal years. For all other business entities, it is effective for fiscal years beginning after 15 December 2029 and interim periods within those fiscal years.
- Entities may apply the guidance using a modified prospective, modified retrospective or retrospective approach. Early adoption is permitted.

Overview

The Financial Accounting Standards Board (FASB or Board) issued a final Accounting Standards Update (ASU) to establish guidance on the recognition, measurement and presentation of a government grant received by a business entity. US GAAP did not provide such guidance, and many business entities have been analogizing to International Accounting Standard (IAS) 20[1] or other guidance when accounting for government grants.

The standard incorporates elements of IAS 20 into US GAAP, modifying certain aspects of that standard's scope, recognition threshold and other implementation guidance. The ASU is intended to reduce diversity and promote greater consistency in the accounting for government grants since business entities will no longer apply other guidance by analogy.

How we see it

Entities that have been applying guidance other than IAS 20 by analogy to account for government grants (e.g., the not-for-profit guidance in ASC 958-605) are generally expected to be impacted the most by the new guidance.

Key considerations

Scope

The guidance applies to all business entities. It does not apply to not-for-profit entities[2] and employee benefit plans in the scope of ASC 960, ASC 962 or ASC 965.

The ASU defines a government grant as a transfer of a monetary asset or a tangible nonmonetary asset, other than in an exchange transaction (including an exchange transaction that may be at a significant discount to fair value), from a government to a business entity. The guidance does not apply to exchange transactions (such as transactions in the scope of ASC 606, *Revenue from Contracts with Customers*), transactions in the scope of ASC 740, *Income Taxes*, the benefit of below-market interest rate loans or government guarantees.

The Board provided examples of government grants that are in the scope of the guidance, including transfers of cash or tangible nonmonetary assets (e.g., buildings, land, equipment), forgivable loans when it is probable certain criteria for forgiveness will be met and refundable tax credits outside the scope of ASC 740. The guidance does not apply to intangible assets or services, a reduction of an entity's liabilities (e.g., a sales, property, payroll or other tax abatement), government participation in the ownership of an entity and contributions to business entities from nongovernmental sources in the scope of ASC 958-605.

An entity cannot recognize a government grant until specific requirements are met.

How we see it

Different terms can be used to describe various types of government assistance, such as grants, awards, subsidies and credits. Therefore, an entity should consider the facts and circumstances to determine whether assistance received from a government meets the ASU's definition of a government grant.

Recognition, measurement and presentation

A business entity cannot recognize a government grant until (1) it is probable that it will comply with the conditions attached to the grant and that the grant will be received and (2) it meets the ASU's recognition guidance for a grant related to an asset or a grant related to income.

The ASU replaces the term "reasonable assurance" used in IAS 20 with "probable." The Board said[3] that reasonable assurance is generally interpreted to be consistent with the term probable as defined in the Master Glossary of the Codification.

Similar to IAS 20, the ASU categorizes government grants as either (1) grants related to assets (i.e., a government grant, or part of a government grant, that is conditioned on the purchase, construction or acquisition of an asset) or (2) grants related to income (i.e., a government grant, or part of a government grant, other than those related to assets).

Grant related to an asset

An entity may elect one of the following approaches to account for a grant related to an asset:

- Under the deferred income approach, the entity separately recognizes and presents the grant as deferred income on the balance sheet as it incurs the related costs that the grant is intended to compensate. The entity recognizes the grant in earnings on a systematic and rational basis over the periods in which it recognizes as expenses the related costs that the grant is intended to compensate (e.g., the useful life of the asset). The entity presents the grant as part of earnings either separately under a general heading, such as other income, or by reducing the related expense (e.g., depreciation, gain or loss on sale, impairment).

- Under the cost accumulation approach, the entity reflects the grant in the carrying amount of the asset on the balance sheet as it incurs the related costs that the grant is intended to compensate. There is no separate subsequent recognition or presentation of the grant proceeds in earnings because they have been reflected in the carrying amount of the asset.

An entity electing the deferred income approach for a grant of a tangible nonmonetary asset (e.g., land) that is determined to be a grant related to an asset initially measures the asset at fair value. An entity electing the cost accumulation approach recognizes the asset at the cost to the entity.

Grant related to income

A grant related to income is recognized in earnings on a systematic and rational basis over the periods in which the entity recognizes as expenses the related costs for which the grant is intended to compensate. The entity presents the grant as part of earnings either separately under a general heading, such as other income, or by reducing the related expense.

How we see it

Similar to IAS 20, the guidance allows for optionality regarding where an entity presents a grant related to an asset or a grant related to income, which could better reflect the economics of the grant and its effect on an entity's business or operations. Entities should adopt a presentation approach and consistently apply it to similar fact patterns.

Disclosures

The guidance requires an entity to comply with the existing annual government assistance disclosure requirements in ASC 832. For a grant related to an asset accounted for under the deferred income approach or a grant related to income, the ASU requires disclosures of the line items on the balance sheet and income statement that are affected by the grant and the amounts applicable to each financial statement line item in the current reporting period. For a grant related to an asset accounted for under the cost accumulation approach, a similar disclosure is required for the balance sheet line items affected by the grant, as well as a disclosure of the useful life of any related depreciable or amortizable asset. These disclosures are only required in the period in which the grant is recognized on the balance sheet.

The guidance also requires disclosure of the fair value of a tangible nonmonetary asset received as a government grant in the period in which the grant is recognized on the balance sheet, regardless of whether the entity applies the deferred income approach or the cost accumulation approach.

Accounting for a government grant in a business combination

The guidance creates an exception to the general recognition and measurement principle of ASC 805, *Business Combinations*, for government grants related to income. If an entity has not fully complied with the conditions of a government grant related to income, an acquirer is required to recognize and measure deferred income based on the government grant model. If the entity has fully complied with the conditions, the acquirer does not recognize deferred income.

All other assets and liabilities related to a government grant acquired in a business combination are recognized and measured at their acquisition-date fair value.[4]

Effective date and transition

The guidance is effective for public business entities for fiscal years beginning after 15 December 2028 and interim periods within those fiscal years. For all other business entities, it is effective for fiscal years beginning after 15 December 2029 and interim periods within those fiscal years.

Early adoption is permitted, including adoption in an interim or annual period for which the entity's financial statements have not been issued or made available for issuance. An entity that adopts the guidance in an interim period will do so as of the beginning of the annual period that includes that interim period.

The guidance may be applied on a modified prospective, modified retrospective or retrospective basis.

Under the modified prospective approach, the guidance is applied to government grants that either are not complete[5] as of the effective date or new government grants that are entered into on or after the effective date. Under the modified retrospective approach, the guidance is applied to government grants that either are not complete as of the beginning of the earliest period presented or are entered into on or after the beginning of the earliest period presented. Under this approach, all prior period results are restated for grants that are not complete through a cumulative-effect adjustment to the opening balance of retained earnings at the beginning of the earliest period presented.

Under the retrospective approach, it is applied to all government grants through a cumulative-effect adjustment to the opening balance of retained earnings at the beginning of the earliest period presented.

Endnotes:

1 IAS 20, *Accounting for Government Grants and Disclosure of Government Assistance*.
2 A not-for-profit entity that receives a government grant applies ASC 958-605.
3 Paragraph BC33 of the ASU's Background Information and Basis for Conclusions.
4 Paragraph BC75.
5 The standard includes guidance to determine when a government grant is complete.