To the Point
FASB – final guidance

FASB allows NFPs to simplify their accounting for goodwill and intangible assets

Electing the alternatives will reduce the cost and complexity of an NFP’s accounting for goodwill and certain intangible assets.

What you need to know

● The FASB issued final guidance that allows NFPs to apply accounting alternatives that simplify the subsequent accounting for goodwill and the accounting for certain intangible assets they acquire.

● NFPs that elect the goodwill accounting alternative will amortize goodwill and perform a one-step impairment test, at either the entity level or the reporting unit level, only when an impairment indicator exists.

● NFPs that elect the intangible asset accounting alternative may recognize fewer intangible assets in an acquisition, and they would be required to elect the goodwill accounting alternative.

● The guidance is effective immediately. NFPs that elect to adopt the alternatives do not have to demonstrate preferability and will follow the alternatives’ transition guidance.

Overview

The Financial Accounting Standards Board (FASB) issued final guidance to allow not-for-profit (NFP) entities to elect accounting alternatives to simplify their subsequent accounting for goodwill and their accounting for certain identifiable intangible assets they acquire in an acquisition. The alternatives were previously available only to private companies.

NFPs that elect the goodwill accounting alternative will amortize goodwill on a straight-line basis over 10 years and perform a one-step impairment test at either the entity level or the reporting unit level only when an impairment indicator exists.
NFPS that elect the intangible asset accounting alternative may recognize and measure fewer intangible assets than they otherwise would in a transaction accounted for under the acquisition method in Accounting Standards Codification (ASC or Codification) ASC 805\textsuperscript{2} (or ASC 958-805\textsuperscript{3}), a reorganization event under ASC 852\textsuperscript{4} or when identifying basis differences for an equity method investment under ASC 323.\textsuperscript{5}

The guidance is part of a broader effort by the FASB to consider the subsequent accounting for goodwill and the accounting for certain identifiable intangible assets. When the FASB issued the private company alternatives,\textsuperscript{6} which were developed by the Private Company Council (PCC), it noted that NFPS and public business entities face the same challenges the alternatives were intended to address. The FASB has a separate project on its agenda to consider amendments to the guidance on these topics. NFPS that are considering electing these accounting alternatives should monitor developments in that project because it could result in changes in the guidance for all entities.

**Key considerations**

The new guidance allows NFPS to elect to apply the goodwill accounting alternative in ASC 350,\textsuperscript{7} and the intangible asset accounting alternative in ASC 805 that were previously available only to private companies. All NFPS, as defined in the Master Glossary of the Codification, including those that are conduit bond obligors, are eligible to apply the guidance.

The new guidance changes only the scope of the alternatives, not any of the provisions.

**Goodwill accounting alternative**

NFPS that elect this accounting alternative will amortize goodwill on a straight-line basis over 10 years or over a shorter period if an NFP can demonstrate that another useful life is more appropriate.

The alternative also simplifies the goodwill impairment test. Upon adoption of the alternative, an NFP is required to make an accounting policy election to test goodwill for impairment at the entity level or the reporting unit level. The NFP also will perform a one-step impairment test only when an event or circumstance indicates that the fair value of the entity (or reporting unit) may be less than its carrying amount (i.e., when a triggering event occurs). An NFP will recognize an impairment for any difference between the fair value of the entity (or reporting unit) and its carrying amount. The amount of the charge is limited to the entity's (or reporting unit's) carrying amount of goodwill.

NFPS that elect to test goodwill for impairment at the entity level will be able to avoid the costly and complex process of identifying reporting units and allocating assets, liabilities and goodwill to them for impairment testing purposes. However, NFPS will still have to allocate impairment to each amortizable unit of goodwill (i.e., goodwill resulting from multiple acquisitions). This will require an NFP to track each amortizable unit of goodwill, regardless of the level at which it tests goodwill for impairment.

Like private companies, NFPS that elect this accounting alternative will have to apply it to all existing goodwill and goodwill recognized in future acquisitions. NFPS that elect this alternative also will be required to comply with its presentation and disclosure requirements.
How we see it
The FASB said in the Background Information and Basis for Conclusions of Accounting Standards Update (ASU) 2019-06 that users of an NFP’s financial statements often disregard goodwill because they are generally more interested in how an NFP carries out its mission, the efficiency of its operations, whether the NFP is sustainable and the NFP’s ability to repay debt. Therefore, simplifying an NFP’s subsequent accounting for goodwill will benefit NFPs without affecting the information users of their financial statements are most interested in.

Intangible asset accounting alternative
An NFP that elects the intangible asset alternative may recognize fewer intangible assets in an acquisition. That is, the only customer-related intangible assets it will recognize are those that are capable of being sold or licensed separately from the other assets of an acquired business. As a result, NFPs that elect the alternative will subsume into goodwill certain types of customer-related intangible assets that they have historically recognized separately. NFPs also will no longer be required to separately recognize acquired noncompetition agreements under the alternative.

Generally, customer-related intangible assets would not meet the criterion for separate recognition because they typically aren’t capable of being sold or licensed separately from other assets. However, ASC 805 lists mortgage servicing rights, commodity supply contracts, core deposits and customer information (e.g., names, contact information) as examples of customer-related intangible assets that could meet this criterion.

ASC 805 also clarifies that contract assets, as defined in ASC 606, and leases are not considered customer-related intangible assets for purposes of applying this accounting alternative and, therefore, they are not eligible to be subsumed into goodwill. Instead, contract assets or lease-related assets or liabilities will continue to be evaluated for recognition.

In some cases, a customer contract may include terms that are favorable or unfavorable relative to market terms (generally referred to as the off-market component). As noted in the Background Information and Basis for Conclusions of ASU 2014-18, the FASB and the PCC agreed that the off-market component of a favorable customer contract is eligible to be subsumed into goodwill because it is an intangible asset. However, the off-market component of an unfavorable customer contract is not eligible to be subsumed into goodwill because it is a liability and, therefore, it is not within the scope of the alternative.

The alternative applies only to noncompetition agreements that an NFP acquired in an acquisition. We believe it does not apply to noncompetition agreements that are entered into contemporaneously with an acquisition and are accounted for separately. As a result, an NFP still needs to initially measure and subsequently account for those noncompetition agreements.

Like private companies, NFPs that elect this alternative are required to also elect the goodwill accounting alternative described above. That’s because the FASB believes that it is inappropriate to subsume finite-lived intangible assets into indefinite-lived goodwill. However, NFPs that elect the goodwill accounting alternative are not required to elect this alternative.

How we see it
We believe this alternative will generally reduce the cost and complexity of an NFP’s accounting for an acquisition because an NFP will not have to determine the fair value of certain customer-related intangible assets and noncompetition agreements or account for them separately.
Transition and effective date

The guidance is effective immediately. An NFP that elects to adopt the alternatives does not have to demonstrate preferability; it will follow the transition guidance the first time it applies them.

The guidance on the goodwill accounting alternative will be applied prospectively for goodwill recognized after the alternative is adopted. The accounting alternative will be applied to existing goodwill as of the beginning of the annual period of adoption, and that goodwill will be amortized prospectively on a straight-line basis. NFPs will apply the intangible asset accounting alternative when the first qualifying transaction occurs after adoption, and the guidance will be applied prospectively. Under the alternative, customer-related intangible assets and noncompetition agreements that exist as of the beginning of the period of adoption are not eligible to be subsumed into goodwill upon adoption of the alternative.

Endnotes:

1 ASU 2019-06, Intangibles – Goodwill and Other (Topic 350), Business Combinations (Topic 805), and Not-for-Profit Entities (Topic 958), Extending the Private Company Accounting Alternatives on Goodwill and Certain Identifiable Intangible Assets to Not-for-Profit Entities.
2 ASC 805, Business Combinations.
3 ASC 958-805, Not-for-Profit Entities – Business Combinations.
4 ASC 852, Reorganizations.
5 ASC 323, Investments – Equity Method and Joint Ventures.
7 ASC 350, Intangibles – Goodwill and Other.
8 ASC 606, Revenue from Contracts with Customers.