

Snapshot

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FASB proposes guidance for revenue contracts acquired in a business combination

The FASB recently [issued](#) proposed ASU, *Accounting for Contract Assets and Contract Liabilities from Contracts with Customers (Topic 805, Business Combinations)*, which would require an acquirer to apply the guidance in ASC 606 when recognizing and measuring contract assets and contract liabilities related to customer contracts acquired in a business combination, instead of recognizing such assets and liabilities at fair value. In addition, the proposal clarifies that all contracts requiring the recognition of assets and liabilities in accordance with the guidance in ASC 606, such as contract liabilities derived from the sale of nonfinancial assets within the scope of ASC 610-20, would fall within the scope of the proposed guidance.

The proposed guidance does not affect the accounting for other assets or liabilities that may arise from revenue contracts from customers in a business combination, such as customer-related intangible assets and contract-based intangible assets, such as off-market contract terms.

According to the proposed ASU, the amount of contract assets and liabilities recognized by the acquirer as of the acquisition date would be same as the amount presented in the acquiree's financial statements immediately prior to the acquisition date, unless one of the following conditions applies:

- The acquiree and acquirer have different revenue recognition policies.
- The acquirer's estimates are different from the acquiree's estimates.

- The acquiree's application of ASC 606 is erroneous.

Contract liabilities

The proposed amendments would require an acquirer to recognize a contract liability if both (1) the acquiree has an unfulfilled performance obligation in a contract with a customer, and (2) the acquiree has been paid or the consideration related to the performance obligation is still due. The guidance in ASC 606 defines a performance obligation as "a promise in a contract with a customer to transfer to the customer either (a) a good or service (or a bundle of goods or services) that is distinct; (b) a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer."

The proposed guidance would generally result in entities recognizing contract liabilities similar to those recognized under the existing legal obligation approach in ASC 805. However, for certain types of performance obligations, such as licenses of symbolic intellectual property or goods or services that are provided as a customary business practice, the proposed amendments are expected to change the current practice, as an acquirer would be required to recognize a contract liability in accordance with ASC 606, while under current guidance in ASC 805, it may not recognize the contract liability using the legal obligation approach.

The guidance in the proposed ASU would require the contract liabilities to be measured as of the acquisition

date, in accordance with the guidance in ASC 606, using the transaction price of the customer contract rather than the fair value of the contract liability.

Contract assets

The proposed ASU requires an acquirer to recognize a contract asset when a performance obligation is either wholly or partially satisfied, but the amount of consideration hinges on a condition other than the passage of time and the consideration is not yet due or has not yet been received.

The guidance in the proposed ASU would require the contract assets to be measured as of the acquisition date, in accordance with the guidance in ASC 606, using the transaction price of the customer contract rather than the fair value of the contract asset.

Transition

An acquirer would apply the proposed guidance from the beginning of the fiscal year of adoption on a prospective basis to business combinations that occur on or after the adoption date.

Early adoption of the proposed amendments would be permitted, including adoption in an interim period.

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