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Viewpoint

Not-for-profit entities: Preparing for year-end financial reporting

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Introduction

Since 2016, not-for-profit entities (NFPs) have been reckoning with an influx of new guidance that directly impacts their financial reporting. The issuance of ASU 2016-14 marked a watershed moment for NFPs, ushering in amendments that completely overhauled how NFPs classify net assets and present financial information, and replacing guidance that had been in place since 1993.

Since then, the FASB has issued several new accounting standards that are designed to enhance the usefulness and transparency of information provided to donors, grantors, and other users of NFP financial statements, as well as to decrease the cost and complexity for NFPs in preparing their financial statements. That guidance includes

- ASU 2020-07 on contributions of nonfinancial assets
- ASU 2019-06 on accounting alternatives for goodwill and intangible assets
- ASU 2019-03 on deaccessions of collections
- ASU 2018-08 on contributions received and contributions made

Compounding this specific guidance, NFPs are wrestling with other major new accounting standards that impact all entities, including NFPs, such as the new leasing standard, along with general accounting and financial reporting issues that could impact an NFP's preparation of its financial statements, such as the accounting alternatives related to subsequent accounting for goodwill.

And, like many companies, NFPs are facing unique challenges driven by COVID-19 and related legislation, such as assessing asset impairments and debt modifications, and how to account for funds received through government programs intended to sustain entities that faced related business disruptions.

This Viewpoint, complete with original FASB citations, flowcharts and tables, as well as insights gleaned from our professionals, helps to unravel the multifaceted financial reporting challenges currently facing NFPs.

1. New accounting pronouncements

1.1 ASU 2020-07: Contributions of nonfinancial assets

ASC 958-605 specifies how an NFP should recognize and measure contributions, but that guidance does not include presentation or disclosure requirements for contributed "nonfinancial assets" (defined below), other than certain disclosure requirements for contributed services. The current guidance in ASC 958-605-50-1 requires NFPs to disclose qualitative information about programs and activities for which contributed services were utilized, along with certain related quantitative disclosures.

Nonfinancial Asset: An asset that is not a financial asset. Nonfinancial assets include land, buildings, use of facilities or utilities, materials and supplies, intangible assets, or services.

Given the significance of contributed nonfinancial assets in practice, the FASB issued ASU 2020-07 in order to increase the transparency surrounding the amount of contributed nonfinancial assets both received and used in an NFP's programs for donors and other financial statement users. The amendments require an NFP to present contributed nonfinancial assets as a line item in the statement of activities, separately from contributed cash and other financial assets; in contrast, legacy guidance offered no prescriptive presentation requirements for contributed nonfinancial assets. Because the term "nonfinancial assets" includes services, as defined in the Master Glossary, the amendments in ASU 2020-07 expand upon the existing disclosure guidance for contributed services by requiring NFPs to separately present contributed services, along with other contributed nonfinancial assets, on the face of the statement of activities, if applicable. The recognition and measurement guidance for contributed services and other nonfinancial assets is not impacted by the new guidance.

Separate presentation is required within changes in net assets both with and without donor restrictions; therefore, an NFP that uses a single-column rather than a multicolumn format in the statement of activities should present contributed nonfinancial assets separately in both the with and without donor restrictions sections, if applicable. Separate expense presentation related to how contributed nonfinancial assets are used is not required, but qualitative information about how the contributions are used is required, as discussed in the following paragraph.

The amendments in ASU 2020-07 introduce incremental disclosure requirements that are codified in ASC 958-605-50-1A, which require an NFP to disclose a disaggregation of the amount of contributed nonfinancial assets by category (for example, property, food, medical supplies, services), along with qualitative information focusing on

- Whether contributed nonfinancial assets were either monetized or utilized during the period and, if utilized, a description of how the assets were used in the NFP's programs or other activities
- The policy, if any, for monetizing rather than using the assets

- A description of (1) any donor-imposed restrictions on the contributed nonfinancial assets, and (2) the valuation techniques and inputs utilized in the fair value measurement of the contributed nonfinancial assets
- The principal or the most advantageous market used to arrive at a fair value measure of the contributed nonfinancial assets if donor-imposed restrictions prohibit the entity from transacting in that market

The new disclosure requirements expand upon the existing disclosure requirements for contributed services, which were otherwise not substantively amended by the amendments in ASU 2020-07.

NFPs need to establish processes to capture the necessary information for the new disclosure requirements, such as whether contributed nonfinancial assets were monetized or utilized during the period. The amendments contain no prescriptive requirements about the number or type of categories of contributed nonfinancial assets that an NFP must disclose on a quantitative basis, but those categories should be decision-useful for donors and support how the entity carries out its mission.

The new presentation and disclosure requirements are effective for all NFPs for annual periods beginning after June 15, 2021 and for interim periods within fiscal years beginning after June 15, 2022. Early application is permitted. The new guidance should be applied retrospectively to all periods presented within the financial statements.

ASC 958-605-45-7A

An NFP shall present contributed nonfinancial assets as a separate line item in the statement of activities, apart from contributions of cash and other financial assets. See paragraph 958-605-50-1A for disclosure requirements for contributed nonfinancial assets.

ASC 958-605-50-1A

A not-for-profit entity (NFP) shall disclose in the notes to financial statements a disaggregation of the amount of contributed nonfinancial assets recognized within the statement of activities by category that depicts the type of contributed nonfinancial assets. For each category of contributed nonfinancial assets, an NFP also shall disclose the following:

a. Qualitative information about whether contributed nonfinancial assets were either monetized or utilized during the reporting period. If utilized, a description of the programs or other activities in which those assets were used shall be disclosed.

b. The NFP’s policy (if any) about monetizing rather than utilizing contributed nonfinancial assets.

c. A description of any donor-imposed restrictions associated with the contributed nonfinancial assets.

d. A description of the valuation techniques and inputs used to arrive at a fair value measure in accordance with paragraph 820-10-50-2(bbb)(1), at initial recognition.

e. The principal market (or most advantageous market) used to arrive at a fair value measure if it is a market in which the recipient NFP is prohibited by a donor-imposed restriction from selling or using the contributed nonfinancial assets.

See paragraph 958-605-50-1B for additional disclosures for contributed services.

1.2 ASU 2021-03: Accounting for goodwill and intangible assets

Over the past few years, the FASB's PCC has provided relief for private entities, including NFPs, when subsequently accounting for goodwill and for recognizing certain intangibles resulting from a business combination. This relief includes accounting alternatives for amortizing goodwill, for evaluating triggering events, and for recognizing certain intangible assets, discussed individually below.

Accounting alternative for amortizing goodwill

Under ASC 350-20-35-63, the accounting alternative for amortizing goodwill allows NFPs to elect to amortize goodwill on a straight-line basis over 10 years or less if a useful life shorter than 10 years is more appropriate, rather than carrying goodwill on the books at its original value and testing it for impairment annually under U.S. GAAP. Further, an NFP electing this alternative must also elect whether to test goodwill for impairment at the entity level or at the reporting unit level.

Under this accounting alternative, impairment testing is performed when a "triggering event" occurs, unless the accounting alternative for evaluating a triggering event under ASU 2021-03 is also adopted (see discussion in "Accounting alternative for evaluating triggering events"). A "triggering event" exists when an event occurs or circumstances change that indicate the fair value might be less than the carrying amount of the reporting unit (or that of the entity if an entity decides to test goodwill at the entity level under ASC 350-20-35-65). If a triggering event occurs, an entity should perform a goodwill impairment test using the triggering event date as the measurement date without the use of hindsight in accordance with ASC 350, unless the entity has adopted the accounting alternative for evaluating triggering events.

ASC 350-20-35-63

Goodwill relating to each business combination, acquisition by a not-for-profit entity, or reorganization event resulting in fresh-start reporting (amortizable unit of goodwill) shall be amortized on a straight-line basis over 10 years, or less than 10 years if the entity demonstrates that another useful life is more appropriate.

Accounting alternative for evaluating triggering events

Prior to the relief provided in ASU 2021-03, NFPs were required to monitor and evaluate triggering events throughout the year to determine whether it is more likely than not that goodwill is impaired. The amendments in ASU 2021-03 allow NFPs to forego monitoring these triggering events during the reporting period and instead require them to perform goodwill impairment evaluations only as of the end of the reporting period, whether that reporting period is on an interim or annual basis. The amendments also allow an entity that has elected to amortize goodwill under the alternative discussed under "Accounting alternative for amortizing goodwill" above to elect the alternative for evaluating impairment triggering events.

Identifying interim reporting dates

While the FASB chose not to define what constitutes a "reporting date," in the Basis for Conclusions to ASU 2021-03, the Board observed that many private companies and NFPs provide some level of financial information more frequently than annually in compliance with the recognition and measurement principles in U.S. GAAP—for example, by providing financial information to lenders, other investors, or regulators. The FASB also observed that it would be "misleading" to users of financial statements to allow entities

providing U.S. GAAP-compliant financial information on an interim basis to delay evaluating goodwill for impairment until the end of the annual reporting period. Accordingly, if an NFP is required (or elects) to provide financial information on an interim basis that complies with the recognition and measurement principles of U.S. GAAP, it would conclude that it has an interim reporting period.

Private entities and NFPs that elect to apply the accounting alternative for goodwill impairment triggering events should carefully evaluate their reporting requirements to determine whether (1) interim-period financial information is reported in compliance with the recognition and measurement principles of U.S. GAAP, and (2) those reporting requirements create an interim reporting date for purposes of applying the accounting alternative. Additionally, an NFP should consider whether financial information reported at an interim date would be affected by goodwill impairment when determining if its reporting requirements create an interim reporting date. If the financial information would not be impacted by goodwill impairment, then an NFP does not have an interim reporting date for the purposes of applying the accounting alternative. If an NFP concludes that it has an interim financial reporting date and elects to apply the accounting alternative, it must evaluate goodwill triggering events as of the end of each interim reporting period in addition to the end of the annual reporting period.

NFPs are required to disclose their election of the accounting alternative under ASU 2021-03 as a significant accounting policy in the notes to their financial statements.

See further discussion of the amendments under ASU 2021-03 in Snapshot 2021-06.

Accounting alternative for recognizing certain intangible assets

The PCC also issued a third accounting alternative, codified in ASC 805-20-25-30, whereby NFPs may choose to no longer recognize certain customer-related intangible assets and noncompetition agreements separately from goodwill. Under this accounting alternative, only noncompetition agreements and customer-related intangible assets that are not capable of being sold or licensed independently from an entity's other assets may be subsumed into goodwill.

ASC 805-20-25-30

An intangible asset is identifiable if it meets either the separability criterion or the contractual-legal criterion described in the definition of identifiable. However, under the accounting alternative, an acquirer shall not recognize separately from goodwill the following intangible assets:

a. Customer-related intangible assets unless they are capable of being sold or licensed independently from other assets of a business

b. Noncompetition agreements.

It is important to note that an NFP that elects this accounting alternative is also required to elect the alternative on amortizing goodwill. However, an NFP electing the goodwill amortization alternative is not required to elect the alternative for recognizing certain intangible assets.

1.3 ASU 2018-08: Contributions received and contributions made

Many NFPs that receive grants and enter into similar contracts with government agencies and other organizations have reported difficulty in determining whether those arrangements should be classified as contributions or exchange transactions, and whether arrangements that qualify as contributions should be

characterized as conditional or unconditional. This lack of clarity resulted in diversity in practice in how NFPs accounted for grants and contracts, which prompted the FASB to issue ASU 2018-08, with a twofold objective:

- To provide a framework for determining whether a particular transaction is an exchange or a contribution, including how to evaluate whether a resource provider receives commensurate value in exchange; and
- To offer guidance to assist entities in determining whether a contribution is conditional or unconditional.

The amendments in ASU 2018-08 apply to both recipients and resource providers.

Fundamental to deciding whether a contribution is conditional or unconditional under the new guidance is determining whether an agreement includes both a "barrier" and either (a) a *right of return* to the resource provider for assets transferred, or (b) a *right of release* for the resource provider from transferring assets in the future. Generally, a "barrier" is a stipulation in an agreement that must be overcome before the recipient is entitled to the assets transferred or promised, and ASC 958-605-25-5D provides a list of indicators to determine whether a barrier exists. If an agreement includes both a barrier and a right of return or right of release, the contribution is deemed conditional. In this case, a recipient should account for amounts received as a liability and recognize contribution revenue only when the condition is met. Similarly, resource providers should not recognize contribution expense until the condition is met.

The amendments in ASU 2018-08 do not impact existing guidance in ASC 958 on whether unconditional contributions are with or without donor restrictions. As a result, a recipient that concludes under the amendments that a contribution is unconditional or that the condition has been met should apply the existing guidance on donor restrictions.

The amendments in ASU 2018-08 have staggered effective dates for resource recipients and resource providers, as shown in Figure 1, although early application is permitted for both parties. Most resource recipients should have already implemented the new guidance, but resource providers, particularly foundations, should comply with the new guidance by recognizing the associated expense for conditional contributions only when the conditions are met.

Figure 1: Effective dates of ASU 2018-08

Type of entity	Apply new guidance as of annual periods beginning after:
Resource recipients – NFPs with conduit debt	June 15, 2018, including interim periods within those annual periods
Resource recipients – All other NFPs	December 15, 2018 and interim periods within annual periods beginning after December 15, 2019
Resource providers – NFPs with conduit debt	December 15, 2018, including interim periods within those annual periods

Type of entity	Apply new guidance as of annual periods beginning after:
Resource providers – All other NFPs	December 15, 2019 and interim periods within annual periods beginning after December 15, 2020

Grant Thornton insight: NFPs that are both a grantor and a grantee

We encourage those NFPs that are both a grantor and a grantee to apply the new guidance to both types of transactions—that is, when the NFP acts as a resource provider and as a resource recipient—as of the same earliest effective date applicable to them, despite the staggered effective dates for resource recipients and resource providers. Doing this will allow NFPs to achieve efficiencies in adopting the new guidance. Additionally, it is useful to financial statement users for the new guidance to be applied to both types of transactions at the same time to improve consistency within the financial statements.

For further discussion, refer to NDS 2018-06, "FASB clarifies scope of contribution accounting."

1.4 ASU 2019-03: Deaccession of collections

Certain NFPs, such as museums, libraries, and art galleries, often possess, maintain, and/or display collection items for the benefit of the public, for example, by offering public exhibitions. Typically, an NFP is required to recognize contribution revenue for donated assets based on the item's fair value. Assets contributed to an existing collection by a donor might include one-of-a-kind or invaluable assets and valuing these items may be complex and costly. Therefore, the guidance in ASC 958-360-25-1 and 25-3 and in ASC 958-605-25-19 aims to reduce the reporting burden on NFPs by providing three alternative accounting policies for reporting collections. Under one alternative, NFPs are neither required to capitalize all collection items nor to recognize revenue for items contributed to a collection if a "collection" meets three specific criteria, as defined in the Master Glossary (see below).

The amendments in ASU 2019-03 broaden the scope of one of the three criteria outlined in the definition of a "collection" by expanding on how proceeds from "deaccessions" (the removal and subsequent sale of an item from a collection) can be used and still qualify as a collection. Under legacy guidance, an entity is permitted to use the proceeds from the deaccession of collection items only to acquire other items for the collection. However, this criterion diverged from the definition of a collection used for accreditation purposes in the *Code of Ethics for Museums,* published by the American Alliance of Museums. As a result, the FASB expanded its definition of a collection in ASU 2019-03 so that the proceeds from deaccessions may be used not only to acquire new collection items, but also for the direct care of existing collection items, or for both purposes. The new definition better aligns U.S. GAAP with industry guidance and, as a result, is expected to reduce diversity in practice.

Collections: Works of art, historical treasures, or similar assets that meet all of the following criteria:

a. They are held for public exhibition, education, or research in furtherance of public service rather than financial gain.

b. They are protected, kept unencumbered, cared for, and preserved.

c. They are subject to an organizational policy that requires the use of proceeds from items that are sold to be for the acquisitions of new collection items, the direct care of existing collections, or both.

Collections generally are held by museums; botanical gardens; libraries; aquariums; arboretums; historic sites; planetariums; zoos; art galleries; nature, science, and technology centers; and similar educational, research, and public service organizations that have those divisions; however, the definition is not limited to those entities nor does it apply to all items held by those entities.

ASC 958-360-25-1

Property, plant, and equipment acquired by contribution is recognized in accordance with the Contributions Received Subsections of Subtopic 958-605. However, a not-for-profit entity (NFP) need not recognize contributions of works of art, historical treasures, and similar assets if the donated items are added to collections (see the following paragraph and paragraph 958-360-25-3).

ASC 958-360-25-2

Works of art, historical treasures, and similar items that are not part of a collection shall be recognized as assets in financial statements.

ASC 958-360-25-3

An NFP that holds works of art, historical treasures, and similar items that meet the definition of a collection has the following three alternative policies for reporting that collection:

a. Capitalization of all collection items

b. Capitalization of all collection items on a prospective basis (that is, all items acquired after a stated date)

c. No capitalization.

Capitalization of selected collections or items is precluded.

ASC 958-605-25-19

An entity need not recognize contributions of works of art, historical treasures, and similar assets if the donated items are added to collections that meet all three of the criteria in the definition of a collection. Contributed collection items shall be recognized as revenues or gains if collections are capitalized and shall not be recognized as revenues or gains if collections are not capitalized. An entity that does not

recognize and capitalize its collections or that capitalizes collections prospectively shall disclose the additional information required by paragraphs 958-360-45-3 and 958-360-45-5.

An NFP's financial statement disclosures should comply with the guidance in ASC 958-360-50-7. Specifically, the NFP must disclose its policy to use proceeds for the acquisition of new collection items or for the direct care of existing collection items, or for both purposes. If proceeds are used for direct care, entities are also required to disclose the types of expenditures that qualify as such.

Grant Thornton insight: The definition of 'direct care' of a collection

The FASB expanded its definition of a "collection" in ASU 2019-03 so that the proceeds from deaccessions may be used both to acquire new collection items and also for the direct care of existing collection items (or for both purposes). However, the Board did not go so far as to define "direct care" and, instead, chose to allow the industry to determine its own definitions, especially after considering all of the different types of collections that entities may hold. As a result, an NFP should establish and/or apply a definition of "direct care" that is consistent with the definition used by its peers, as a significant difference might reduce the comparability of its financial statements.

The amendments in ASU 2019-03 are effective for all NFPs in annual periods beginning after December 15, 2019 and in interim periods within fiscal years beginning after December 15, 2020. Early application is permitted, and the new guidance should be applied prospectively.

ASC 958-360-50-7

A collection-holding NFP shall disclose its organizational policy for the use of proceeds from deaccessioned collection items, including whether those proceeds could be used for acquisitions of new collection items, the direct care of existing collections, or both. If the collection-holding entity allows proceeds from deaccessioned collection items to be used for direct care, the entity shall disclose its definition of direct care.

1.5 ASU 2018-15: Accounting for cloud computing arrangements

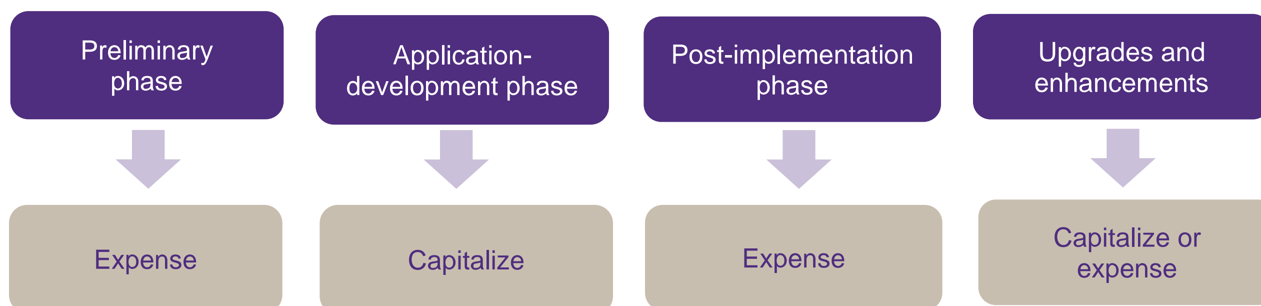
Many entities, including NFPs, are using cloud computing arrangements in place of on-site software, which often involves significant up-front implementation costs. Because of a lack of specific guidance on how to account for those implementation costs, diversity in practice has developed over the years.

In 2018, the FASB issued ASU 2018-15, which provides guidance on accounting for costs incurred by a customer when implementing a cloud computing (or "hosting") arrangement that is considered a service contract. The amendments, which are codified in ASC 350-40, allow an NFP that incurs costs to implement a cloud computing arrangement to account for those costs similar to costs for internal-use software. In other words, NFPs should consider both the *nature* of these costs and the *phase of development* in which they are incurred to determine whether the costs should be capitalized or expensed. Under ASC 350-40, costs related to implementation activities performed in the preliminary and

post-implementation phases of a project are expensed as incurred, while costs related to developing internal-use computer software during the application development phase are generally capitalized (see Figure 2). NFPs that incur costs to upgrade or enhance existing software should either capitalize or expense the costs, depending on the type of cost involved. Those implementation costs that meet the capitalization requirement should be recognized over the term of the hosting arrangement.

Hosting Arrangement: In connection with accessing and using software products, an arrangement in which the customer of the software does not currently have possession of the software; rather, the customer accesses and uses the software on an as-needed basis.

Figure 2: Accounting for costs incurred for internal-use software



For NFPs, the amendments in ASU 2018-15 are effective for annual periods beginning after December 15, 2020 and for interim periods within annual periods beginning after December 15, 2021. Early adoption is permitted in any annual or interim period if the financial statements have not been issued or been made available for issuance.

NFPs should apply the amendments either (1) retrospectively, recognizing the cumulative effect of applying the amendments in the opening net assets of the earliest period presented in the financial statements, or (2) prospectively to costs for activities performed on or after the adoption date of the amendments.

1.6 ASU 2016-02: Leases

The amendments in ASU 2016-02, which overhaul the existing lease guidance, have triggered profound financial reporting changes for all entities with leasing contracts, including NFPs. These amendments now require lessees to recognize operating leases on the statement of financial position, rather than solely disclosing operating lease commitments in the footnotes. Codified in a new Topic, ASC 842, the amendments do not impact how lease expense is recognized in the statement of activities, as lessees still classify leases either as operating leases, for which straight-line rent expense is recognized, or as finance leases (“capital” leases under legacy guidance), for which interest and amortization expense are recognized. While the new guidance also changes certain aspects of lessor accounting, the remaining discussion focuses on changes for lessees.

Given that the new leasing guidance now requires lessees to record most leases on the statement of financial position, it is critical for NFPs to identify all of their arrangements that meet the definition of a "lease," which is defined as the right to control the use of an identified asset for a period of time. If the criteria that define a lease are met, then the lease should generally be recognized on the statement of financial position. Contracts to be evaluated, both when transitioning to ASC 842 and on an ongoing basis, should include any known operating leases (for example, office leases), as well as any "embedded" leases, which is the use of property, plant, or equipment that is incorporated into a service contract (for example, leased computer hardware and associated maintenance services that are contracted for on a combined basis). While an NFP may have historically recognized the cost of the service contract as an operating expense in its statement of activities, after adopting ASC 842, the NFP must determine whether it controls an identified asset within its service contracts for the contractual term and, if so, record payments made to lease the asset on the statement of financial position as a lease liability, along with an associated right-of-use asset.

Contract: An agreement between two or more parties that creates enforceable rights and obligations.

Lease: A contract, or part of a contract, that conveys the right to control the use of identified property, plant, or equipment (an identified asset) for a period of time in exchange for consideration.

In ASU 2020-05, the FASB revised the effective dates of ASC 842 for certain NFPs with conduit debt and for all other NFPs to provide financial reporting relief from the impact of COVID-19. As revised, ASC 842 is effective for NFPs with conduit debt for annual periods beginning after December 15, 2018 and for interim periods within those periods, unless the NFP did not issue, or make available for issuance, its financial statements as of June 3, 2020, in which case, the NFP may adopt ASC 842 for annual periods beginning after December 15, 2019 and for interim periods within those periods. All other NFPs are required to adopt ASC 842 for annual periods beginning after December 15, 2021 and for interim periods within fiscal years beginning after December 15, 2022. Early adoption is permitted for all entities.

Practical expedients

To facilitate the transition from the legacy guidance to the new leasing guidance, ASC 842 provides several practical expedients that entities may elect when they initially apply the new guidance. One option that entities commonly elect when transitioning to ASC 842 is a package of expedients that allows them to forgo reassessing certain conclusions (listed below) reached under legacy U.S. GAAP. All expedients in this package must be applied together for all leases that commence before the effective date of ASC 842, as amended. In transitioning to ASC 842, an entity electing this package of practical expedients would not need to assess all of the following:

- Whether any expired or existing contracts are leases or contain leases
- How expired or existing leases are classified
- Whether unamortized initial direct costs for existing leases meet the narrowed definition of initial direct costs under the new guidance

This package of expedients effectively allows an entity to "run off" existing leases, meaning that an entity may continue to account for existing leases based on judgments made under legacy U.S. GAAP. The expedients are not intended to grandfather incorrect assessments made under legacy U.S. GAAP. Therefore, if an entity identifies an error, it should be corrected in accordance with ASC 250.

Another expedient that is available, both upon transition and on an ongoing basis, allows entities not to recognize operating leases on the statement of financial position if the original total lease term is 12 months or less (a "short-term" lease). An entity is required to consider any optional renewal periods or purchase options and whether they are reasonably certain to be exercised when determining whether a lease qualifies for this expedient. While relief is provided from a recognition perspective, an NFP must still comply with the disclosure requirements for short-term leases under ASC 842, particularly the requirement to disclose when short-term lease expense for a period does not reasonably reflect the NFP's short-term lease commitments (for example, payments for a new short-term equipment lease that is material to the financial statements would begin in the next fiscal year).

Transition methods and implementation

An entity may transition to ASC 842 using one of two methods. Under the *modified retrospective* method, an entity applies the transition guidance in ASC 842 as of the beginning of the earliest period presented in the financial statements that reflect the adoption of ASC 842. Under this method, a cumulative-effect adjustment is recorded to net assets as of the beginning of the earliest period presented. Under the *current-period adjustment* method, an entity applies ASC 842 as of the beginning of the period when it adopts ASC 842. Under this method, a cumulative-effect adjustment is recorded to net assets as of the beginning of the period in which ASC 842 is adopted. While the modified retrospective method may improve comparability between reporting periods, NFPs might benefit from using the current-period adjustment method, because any leases that expire before the beginning of the period in which ASC 842 is adopted are not required to transition to the new guidance in ASC 842.

Grant Thornton insight: ASC 842 implementation may require significant effort

Even though the FASB delayed the effective date of ASC 842 for certain NFPs, these entities are still encouraged to begin the adoption process sooner rather than later in case complexities arise in gathering the appropriate documentation, reviewing existing lease agreements, and understanding accounting positions taken under legacy lease guidance. In addition, the search for embedded leases to ensure the completeness of the entity's lease population may require significant effort and collaboration among the various departments in an organization.

It is also important for NFPs to communicate with creditors as part of their adoption process, as financial ratios and, accordingly, loan covenants may be impacted by the balance-sheet recognition of right-of-use assets and lease liabilities upon adoption.

For a comprehensive discussion of the new leasing guidance, refer to Grant Thornton's guide titled *Leases – Navigating the guidance in ASC 842.*

Rent concessions – COVID-19 relief

As a result of the COVID-19-related shift in how real estate is being used, such as scaling back on office space, a significant number of lessees and lessors have recently negotiated rent concessions. For example, lessors might have deferred a lessee's rental payments to a future period or forgiven rental payments altogether for a stated period. Any change to contractual lease payments triggers application of the lease modification guidance in both ASC 842 and ASC 840, which could be burdensome for entities given the number of concessions that occurred due to COVID-19.

In 2020, the FASB staff released a Q&A to provide interpretive guidance that addresses certain frequently asked questions about accounting for lease concessions related to COVID-19. According to the Q&A, the staff believes that under both ASC 842 and ASC 840, if the new leasing guidance is not yet adopted, an entity may elect to treat qualifying lease concessions as if they were based on enforceable rights and obligations within the existing contract and, as a result, may forgo applying modification accounting to those concessions. As a result, this election allows an entity to skip a detailed review of each lease to determine whether the lessee has an enforceable right to each concession. According to the FASB staff Q&A, qualifying concessions must meet both of the following criteria: (1) the concession is related to COVID-19, and (2) there is not a substantial increase in the lessee's obligations or the lessor's rights under the contract.

For further discussion, refer to Grant Thornton's Snapshot 2020-15, "Accounting for rent concessions."

1.7 ASU 2020-04: Reference rate reform

Regulators in various jurisdictions around the world have undertaken reference rate reforms to identify interest-rate benchmark rates that are more observable or transaction-based (and therefore are less susceptible to manipulation) than certain interest-rate benchmark reference rates that are commonly used, including the most prominent of them all, LIBOR. Most regulators have agreed to phase out the old rates by December 31, 2021. The discontinuation of benchmark reference rates will require entities to modify contracts that use those rates by replacing the old rates with new rates.

In response to these developments, the FASB issued ASU 2020-04, which adds a Topic to the Codification, ASC 848, for a limited period of time, offering entities certain practical expedients and exceptions from applying modification accounting to contracts modified for reference rate reform if certain criteria are met. The new amendments are designed to reduce operational challenges that entities will face in applying modification accounting to contracts that need to be revised due to ongoing reference rate reforms.

The guidance in ASC 848 does not apply to any contract modifications made after December 31, 2022 or to any hedging relationships entered into or evaluated after December 31, 2022, except for those hedging relationships existing as of December 31, 2022 for which an entity has elected certain optional expedients that are retained through the end of the hedging relationship.

The FASB also clarified in ASU 2021-01 that certain expedients available under ASC 848 for contract modifications and hedge accounting apply to derivatives that use an interest rate for margining, discounting, or aligning a contract price that will be modified as a result of reference rate reform, even if the derivative instrument does not explicitly reference a rate that is expected to be discontinued.

Refer to NDS 2020-08, "Reference rate reform," for further discussion of the amendments under ASU 2020-04.

Grant Thornton insight: Common instruments that reference LIBOR

Financial instruments that are most prevalent among NFPs that reference LIBOR include certain tax-exempt debt issuances and interest rate swap agreements, both of which likely have maturity terms that extend well into the future. Therefore, an NFP should not delay evaluating these and other financial instruments and LIBOR-based contracts for the impact of reference rate reform since the

guidance in ASC 848 offers entities certain practical expedients and exceptions from applying contract modification accounting only for a limited period of time.

1.8 ASU 2018-13: Fair value measurement disclosures

In 2018, the FASB issued ASU 2018-13 to improve the disclosures for fair value measurements under ASC 820 for all entities. These changes impact the financial statements of NFPs with fair value measurements and include significant changes to disclosures involving Level 3 investments, for transfers between Level 1 and Level 2 investments, and for certain calculations of NAV. For NFPs, the following disclosure requirements were modified by these amendments:

- In lieu of a rollforward for Level 3 fair value measurements, entities should disclose transfers into and out of Level 3 of the fair value hierarchy, as well as purchases and issues of Level 3 assets and liabilities for the reporting period.
- For investments in certain entities that calculate NAV, entities should disclose the timing of liquidating an investee's assets and the date when restrictions from redemption might lapse *only* if the investee has communicated the timing to the reporting entity or announced the timing publicly. If the timing is unknown, the reporting entity should disclose that fact.
- For recurring fair value measurements categorized within Level 3 of the fair value hierarchy, entities should provide a narrative description of the uncertainty of the fair value measurement from the use of significant unobservable inputs if those inputs reasonably could have been different at the reporting date. The amendments clarify that the purpose of the measurement uncertainty disclosure is to communicate this information as of the reporting date and is not related to changes in the future.

Further, the amendments removed the requirement to disclose the amount of, and the reasons for, transfers between Level 1 and Level 2 in the fair value hierarchy.

The amendments in this ASU are effective for NFPs with annual periods beginning after December 15, 2019 and should be applied retrospectively to all periods presented in the financial statements.

2. Reminders about existing guidance

2.1 Presentation of financial statements

In 2016, the FASB released ASU 2016-14, with the goal of improving NFP financial statements by providing more useful information to donors, grantors, creditors, and other financial statement users. The amendments significantly change how NFPs present net assets on the face of the financial statements and require additional disclosures for expenses by nature and function, as well as for the liquidity and availability of resources.

ASU 2016-14 represents the first major change to NFP financial statement presentation since the mid-1990s and marks the completion of the first phase of the FASB's project related to NFP financial reporting. The second phase of the project is focused on defining the term "operations" and on aligning the presentation of measures of operations in the statement of activities with measures of operations presented in the statement of cash flows.

Net asset classifications

The most significant change resulting from the amendments in ASU 2016-14 transforms the face of NFP financial statements. NFPs are now required to present two net asset classes (net assets with donor restrictions and net assets without donor restrictions) rather than three net asset classes (unrestricted, temporarily restricted, and permanently restricted).

Net assets are reported separately for those net assets subject to donor-imposed restrictions from those net assets not subject to donor-imposed restrictions. This distinction is important, and donor stipulations are the only factor to use in determining how net assets are classified. Consistent with current guidance, management, the board of directors, or another governing body is not able to classify a gift as donor-restricted, unless the donor makes it a condition of his/her gift. Further, a board-designated endowment is classified as, and included in, net assets without donor restrictions.

The two required net asset classes represent the minimum disaggregation of assets. An NFP may choose to further disaggregate net assets into additional subclasses, such as those expected to be maintained in perpetuity, those spent over time, or those spent for a particular purpose. However, under ASC 958-210-45-1, NFPs are required to report the total for each of the two net asset classes and the total amount of net assets on the statement of financial position.

ASC 958-210-45-1

A statement of financial position shall focus on the not-for-profit entity (NFP) as a whole and shall report all of the following amounts:

a. Total assets

b. Total liabilities

c. Total net assets

d. Total net assets with donor restrictions

e. Total net assets without donor restrictions

f. [Subparagraph superseded by Accounting Standards Update No. 2016-14].

For the statement of activities, the amendments in ASU 2016-14 permit flexibility in the presentation of the information, provided the requirements are met. In other words, under ASC 958-20-55-10, the information may be presented in a single column, in multiple columns, or in two separate statements (for example, a summary statement of changes in net assets without donor restrictions followed by a statement of changes in net assets, including net assets with donor restrictions).

Disclosures for donor restrictions and board designations

The two-class net asset classification system in ASC 958-205-05-6B does not eliminate the requirement to disclose the various types of donor-imposed restrictions. NFPs should report separate line items within net assets with donor restrictions, or they should include this information in the notes to the financial statements, to distinguish between the types of donor-imposed restrictions, including those that are perpetual in nature. Types of donor restrictions to be disclosed might include, but are not limited to, the following restrictions:

- Support for a particular operating activity
- Investment for a specified term
- Use in a specified period
- Acquisition of long-lived assets

ASC 958-205-05-6B

The two required net asset classes (with donor restrictions and without donor restrictions) are a minimum classification scheme, if they are applicable. An NFP can choose to further disaggregate the two net asset classes. For example, an NFP may wish to disaggregate net assets with donor restrictions between those expected to be maintained in perpetuity and those expected to be spent over time or for a particular purpose. However, paragraph 958-210-45-1 does require that the amounts for each of the two classes of net assets and the total of net assets be reported in a statement of financial position.

Additionally, NFPs are required to disclose information about the nature and amounts of different types of restrictions that impact how and when, if ever, the donor-restricted net assets may be used. The amendments in the ASU also require disclosures about the amounts and purposes of board designations of net assets without donor restrictions. Any governing board actions that result in self-imposed limits on the use of resources should also be disclosed in the notes to the financial statements or on the face of the statement of financial position.

Placed-in-service approach

Under ASC 958-205-45-12, NFPs are required to use the placed-in-service approach for reporting the expiration of donor-restricted assets. This approach requires an entity to reclassify the full gift amount from net assets with donor restrictions to net assets without donor restrictions when the acquired or constructed asset is placed in service. This guidance applies to both purpose-restricted contributions of long-lived assets for which the donor does not stipulate how long the assets must be used, and to the contribution of cash or similar liquid assets restricted for the acquisition or construction of long-lived assets.

ASC 958-205-45-12

Unless donor stipulations limit the use of the assets for a period of time or for a particular purpose, donor restrictions on long-lived assets, if any, or cash to acquire or construct long-lived assets are considered to have expired when the assets are placed in service.

The guidance in ASC 958 includes an exception to the placed-in-service requirement if a donor restriction extends beyond the point when the asset is placed in service. For example, if a donor specifies that the acquired property, plant, or equipment must be used for a specified period of time, the restriction would expire over the period of time as the asset is used.

Functional expenses

The guidance in ASC 958-720-45-2 requires NFPs to present an analysis of expenses by both natural classification and functional classification in one location in the financial statements, whether in the notes or in a separate financial statement, so that current and prospective donors may know how resources are being used.

ASC 958-720-45-2

To help donors, creditors, and others in assessing an NFP’s service efforts, including the costs of its services and how it uses resources, a statement of activities or notes to financial statements shall provide information about expenses reported by their functional expense classification, such as major classes of program services and supporting activities, for example:

a. Program services

b. Supporting activities, which often include one or more of the following:

    1. Management and general activities

    2. Fundraising activities

    3. Membership development activities.

Expenses are disaggregated by functional expense category, for example, by major classes of program services and supporting activities. Within each functional class, expenses should be further disaggregated by their natural expense classifications, such as salaries, rent, supplies, and depreciation. Investment expenses, gains and losses, or other items that for-profit entities typically report in other comprehensive income should not be included in this expense analysis, according to the guidance in ASC 958. Furthermore, a qualitative description of the method(s) used to allocate expenses among programs and support functions should be included in the notes to the financial statements.

Investment returns

The amendments in ASU 2016-14, as reflected in ASC 958-220-45-14, also require NFPs to report investment returns net of related investment expenses, including both external and direct internal investment expenses. The purpose of this requirement is to provide a more comparable measure of investment returns across all NFPs, regardless of whether their investment activities are managed by internal staff or outside investment managers. The amendments also eliminate the difficulties and related costs of identifying and separately accounting for embedded fees often included in investment vehicles, such as mutual funds and hedge funds. The net presentation of investment returns means that expenses are included in the net asset categories in which investment returns are reported—that is, net assets with or without donor restrictions.

According to ASC 958-220-45-15, direct internal investment expenses are those involved in the direct conduct or supervision of strategic and tactical activities that generate investment returns. These activities may include salaries, benefits, travel, or other personnel costs incurred by individuals responsible for the development and execution of the investment strategy, as well as costs associated with investment management or with the supervision, selection, and monitoring of external investment management firms. Direct internal investment expenses do not include items that do not directly contribute to generating investment returns, such as costs associated with unitization or other similar aspects of endowment management.

Grant Thornton insight: Allocating internal costs

NFPs are advised to exercise caution when allocating costs to investment expenses under the amendments in ASU 2016-14. Direct internal investment expenses are narrowly defined in the amendments and should include only those expenses that directly contribute to generating investment returns. For example, these costs would not include allocated general and administrative costs, such as bookkeeping or accounting functions.

An NFP is permitted to report investment returns on separate line items by portfolio if each line item relates to a portfolio that is either managed differently or derives its investments from different sources. For example, net returns on invested operating cash may be presented separately from net returns on endowments. Additionally, amounts of net investment returns appropriated for spending should be separately presented from returns in excess of amounts appropriated for spending.

Disclosure requirements – qualitative and quantitative

To further enhance the usefulness of the financial statements, the amendments in ASU 2016-14 require disclosures of qualitative and quantitative information about the NFP’s liquidity and the availability of its resources.

The amendments in ASU 2016-14 require NFPs to qualitatively describe in the notes to the financial statements information that is useful in assessing the liquidity of resources or the maturity of assets and liabilities. NFPs are required to describe in the notes how they intend to manage liquid resources that are available to meet cash needs for general expenditures within one year of the date of the statement of financial position. In addition, NFPs must quantitatively disclose the availability of financial assets at the date of the statement of financial position to meet cash needs for general expenditures within one year of the date of the statement of financial position.

The quantitative information may be disclosed either in the notes or on the face of the statement of financial position. Additional information about liquidity should also be provided by, for example, classifying assets and liabilities as current and noncurrent or sequencing assets and liabilities based on nearness of conversion to cash or reaching maturity. Additional qualitative information should be included in the notes, as necessary, such as information about the availability of financial assets due to their nature; external limits imposed by donors, laws, and contracts; and internal limitations.

Other reporting changes

Although the FASB decided to continue to allow NFPs to choose either the direct or indirect method of reporting cash flows, the amendments remove the requirement to provide a reconciliation to the indirect method when the direct method is used.

For more detailed discussion on ASU 2016-14, refer to NDS 2016-11, "FASB amends NFP financial statement presentation."

2.2 Endowment funds

In general, endowment funds can be established by either donors or a governing board and must be reported in the statement of financial position based on the existence or absence of donor-imposed restrictions. Under ASC 958-205-45, contributed funds with stipulations to invest the donated resources either for a long, specified period of time or in perpetuity are considered donor-restricted endowment funds and should be reported within net assets with donor restrictions in the statement of financial position. If a governing board designates or earmarks portions of net assets without donor restrictions to be invested for a long, but not necessarily specified, time period, these funds are considered board-designated endowment funds and should be reported within net assets without donor restrictions in the statement of financial position.

Although rare, a board-designated endowment fund might include a portion of net assets with donor restrictions that are not restricted for investment in perpetuity. For example, if an NFP receives a contribution restricted for a particular purpose but is unable to spend the contribution in the near term, then the board might decide to categorize such funds for long-term investment.

Investment returns on donor-restricted endowment funds generally are considered free of donor restrictions, unless their use is limited by a donor-imposed restriction or by law. In the United States, most donor-restricted endowment fund earnings are subject to UPMIFA, which extends the donor's restriction to the investment return until the funds are appropriated for expenditure by the governing board. As a result, these returns must be reported within net assets with donor restrictions in the statement of financial position until appropriated for expenditure following the guidance in ASC 958-205-45-13B. Upon appropriation, the restriction expires, as long as all time and purpose restrictions have been met.

An "underwater endowment fund" is a donor-restricted fund whose fair value has fallen below either the original gift amount or the amount required to be maintained by the donor or by law. ASC 958-205-45-13H requires the accumulated losses to be included together with the related fund in net assets with donor restrictions.

Underwater Endowment Fund: A donor-restricted endowment fund for which the fair value of the fund at the reporting date is less than either the original gift amount or the amount required to be maintained by the donor or by law that extends donor restrictions.

In addition, ASC 958-205-50 requires enhanced disclosures for underwater endowment funds, including

- The governing board's interpretation of the relevant state UPMIFA law as to the NFP's ability to spend from underwater endowment funds
- The NFP's policy, and any actions taken during the period, concerning the appropriation of underwater endowment funds
- The aggregate amounts of the following items:
  - Fair value of underwater endowment funds
  - Original endowment gifts or levels that must be maintained by donor stipulation or by law
  - Amount of funds' deficiencies (that is, fair value less original endowment gifts or levels to be maintained)

2.3 Presentation of restricted cash

Under ASC 230, an NFP is required to include amounts generally described as restricted cash and restricted cash equivalents with cash and cash equivalents when reconciling the total amounts shown at the beginning and end of a reporting period on the statement of cash flows. Before the amendments in ASU 2016-18, there was no specific guidance on how to classify and present changes when direct cash receipts were included in restricted cash or restricted cash equivalents, or when direct cash payments were made from restricted cash or restricted cash equivalents, resulting in diversity in practice.

The amendments in ASU 2016-18 require entities to explain, in the statement of cash flows, changes in the totals of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents that occur during the reporting period; however, the amendments do not require entities to report transfers between cash, cash equivalents, and amounts described as restricted cash or restricted cash equivalents as cash flow activities in the statement of cash flows. Internal cash transfers are not part of an entity's operating, investing, and financing activities, and details of those transfers are not reported as cash flow activities in the statement of cash flows.

In addition to the presentation requirements under ASC 230-10, NFPs should also follow the disclosure requirements on restricted cash and restricted cash equivalents under ASC 230-10-50-7 and 50-8.

ASC 230-10-50-7

An entity shall disclose information about the nature of restrictions on its cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. An entity within the scope of Topic 958 on not-for-profit entities also shall provide the disclosures required in paragraph 958-210-50-3.

ASC 230-10-50-8

When cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents are presented in more than one line item within the statement of financial position, an entity shall, for each period that a statement of financial position is presented, present on the face of the statement of cash flows or disclose in the notes to the financial statements, the line items and amounts of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents reported within the statement of financial position. The amounts, disaggregated by the line item in which they appear within the statement of financial position, shall sum to the total amount of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents at the end of the corresponding period shown in the statement of cash flows. This disclosure may be provided in either a narrative or a tabular format.

ASC 958-205-55 provides helpful implementation guidance for NFPs on the statement of cash flows presentation required in ASC 958-230 and ASC 230, including a comprehensive example of illustrative financial statements and footnote disclosures.

3. COVID-19 accounting impacts

3.1 Accounting for asset impairments

An NFP that experiences significant disruption to its operations or other significant changes due to COVID-19 is required to assess its assets for indicators of impairment.

Long-lived assets

An NFP should apply the guidance in ASC 360-10-35-31 to evaluate a long-lived asset “for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable.” NFPs should also consider whether the direct or indirect impact of COVID-19 constitutes an event that would require testing long-lived assets for recoverability. Those events might include

- A significant decrease in the market price of the long-lived assets
- A significant adverse change in the extent or manner in which long-lived assets are being used or their physical condition
- A significant adverse change in the business climate that could affect the value of the long-lived assets

The impairment requirements in ASC 360 also apply to right-of-use assets recognized by lessees on leasing transactions accounted for under ASC 842. Refer to Section 1.6 on accounting for operating leases on the balance sheet under ASC 842.

Inventories

For NFPs that hold inventory, the guidance in ASC 330 specifies two approaches for remeasuring inventory, depending on the cost method applied. In the first approach, inventory is remeasured using the lower of cost or net realizable value. This method is used for all cost methods other than LIFO or the retail method and is widely applicable because many entities use the FIFO or average cost methods. The second approach is the lower of cost or market method that applies only when using LIFO or the retail method.

ASC 330 identifies a variety of possible circumstances that may require the remeasurement of inventory, including obsolescence and physical deterioration. For some NFPs, disruption of the supply chain or decreased demand associated with COVID-19 might have caused inventory obsolescence and deterioration, which would require remeasurement.

ASC 270 specifies that any loss resulting from remeasuring inventory in an interim period should be recognized in the interim period in which the loss occurs. Recoveries that occur in later interim periods within the same fiscal year should be recognized as gains in the interim period in which they occur, but should not exceed previously recognized losses. In addition, if an NFP can reasonably expect to restore a decline in inventory in an interim period within the same fiscal year, the temporary decline does not need to be recognized at the interim date. However, entities may not recognize recoveries related to impairments recognized in previous fiscal years.

Debt and equity securities

NFPs may invest in debt and equity securities subject to fair value measurements under ASC 820. ASC 958-320-35-1 states that all debt securities should be subsequently measured at fair value in the statement of financial position, with changes in value recognized in the statement of activities. Therefore, any impairment losses are captured in the fair value remeasurements.

NFPs with equity securities should generally follow the fair value guidance under ASC 321 for fair value measurements. However, equity securities without a readily determinable fair value that do not qualify to be measured using the practical expedient to estimate fair value at NAV may be eligible for a measurement exception under the amendments in ASU 2016-01, which were codified in ASC 321. The measurement exception allows those investments to be measured at cost, minus impairment if any, plus or minus changes resulting from observable price changes in orderly transactions for an identical or a similar investment of the same issuer. Equity investments that are measured using the measurement exception should be qualitatively evaluated for impairment at each reporting period. The impairment indicators include

- A significant deterioration in the earnings performance, credit rating, asset quality, or business prospects of the investee
- A significant adverse change in the regulatory, economic, or technological environment of the investee
- A significant adverse change in the general market condition of either the geographical area or the industry in which the investee operates
- Factors that raise significant concerns about the investee’s ability to continue as a going concern

Given the significant economic impact of COVID-19, it is likely that equity securities for which the measurement exception has been elected may have qualitative indicators of impairment. If a qualitative assessment indicates that an equity investment is impaired, the entity should measure the equity investment’s fair value and record the difference between that fair value and the carrying value of the equity investment as an impairment loss within changes in net assets.

3.2 Accounting for debt modifications, extinguishments, and TDRs

An NFP whose operations were significantly impacted by COVID-19 may have asked their lenders for temporary payment deferrals; modifications to, or waivers of, violations of debt covenants; or changes to other terms of their debt agreements. Such accommodations qualify as debt modifications and should be carefully evaluated to determine the appropriate accounting treatment.

When determining how to account for a liability modification, an entity should first consider whether the modification is a TDR. ASC 470-60 specifies that a restructuring is a TDR if two conditions are met:

- The borrower is experiencing financial difficulty.
- The lender grants a concession.

A lender grants a concession if the borrower’s effective interest rate on the restructured debt is less than the effective interest rate of the debt immediately before the restructuring. If the restructuring results in a TDR, the borrower should perform the following steps:

- Determine the contractual cash flows of the restructured debt.

- If the total cash flows on the restructured debt are less than the carrying amount of the debt, reduce the carrying amount of the debt to the total contractual cash flows and recognize the reduction in the carrying amount of the debt as a gain on debt extinguishment.
- If the total cash flows on the restructured debt are greater than the carrying amount of the debt, determine a new effective interest rate that equates the total contractual cash flows to the carrying amount of the debt.

If the restructuring is not a TDR, an NFP should instead consider the modification and extinguishment guidance in ASC 470-50. Under that guidance, a liability associated with term debt is considered extinguished if the present value of the cash flows on the restructured debt differs by 10 percent or more from the present value of the cash flows on the original debt, with each set of cash flows discounted using the effective borrowing rate associated with the original debt. If the restructuring does not result in an extinguishment of the original debt, then the entity should determine a new effective borrowing rate on the restructured debt and apply that new rate prospectively.

3.3 Rent concessions

As previously discussed, the FASB staff released a Q&A document to assist entities in accounting for the vast number of rent concessions that occurred due to COVID-19. Refer to Section 1.6 for further discussion.

3.4 Accounting for PPP funds

The 2020 CARES Act, as amended, earmarked over $600 million through the PPP, administered by the SBA, for potentially forgivable loans to support eligible small businesses impacted by COVID-19. The loans, which have a two- or five-year term (depending upon when they were issued) and bear interest at 1 percent, are provided through SBA-approved lenders to an eligible entity. The PPP was closed to additional small business applicants on August 8, 2020.

There are two alternative accounting models that an NFP can apply to account for PPP proceeds. Under the first model, an NFP would account for the proceeds as debt in accordance with ASC 470 and use the effective interest method to accrue interest. The NFP would then apply ASC 405 to determine when to derecognize the liability either (a) upon forgiveness of the debt when the debtor is “legally released,” with a corresponding gain upon extinguishment, or (b) upon repayment of the debt if it is ultimately not forgiven.

Under the second accounting model, the NFP would record the receipt of PPP funds as a nonexchange transaction under ASC 958-605, as the government does not receive commensurate value in exchange for those loans. In accordance with ASC 958-605-25-5A, the contribution would be conditional given the existence of a barrier to incur qualifying expenses, and the borrower would be required to return the funds (that is, repay the loan) if it does not meet the conditions to incur qualifying expenses and comply with other program guidelines. As a result, an NFP would recognize any cash received as a refundable advance until the conditions have been either substantially met or explicitly waived by the donor (or lender in this case) in accordance with ASC 958-605-25-5F. Judgment may be required to determine whether an NFP incurs qualifying expenses and whether the amount received will be forgiven in order to recognize contribution revenue as expenses are incurred over time.

ASC 958-605-25-5A

A donor-imposed condition must have both:

c. One or more barriers that must be overcome before a recipient is entitled to the assets transferred or promised

d. A right of return to the contributor for assets transferred (or for a reduction, settlement, or cancellation of liabilities) or a right of release of the promisor from its obligation to transfer assets (or reduce, settle, or cancel liabilities).

ASC 958-605-25-5F

A transfer of assets that is a conditional contribution shall be accounted for as a refundable advance until the conditions have been substantially met or explicitly waived by the donor.

3.5 Accounting for SVOG funds

The SVOG program was established by the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act, as amended by the American Rescue Plan Act, and is administered by the SBA's Office of Disaster Assistance. The SVOG program, which officially opened in April 2021, includes over $16 billion in grants to be provided to eligible entities with venues that were forced to close due to COVID-19.

NFPs that are eligible to apply to the program include museums, performing arts organizations, or other live venue operators that were in operation as of February 29, 2020. If the entity received a PPP loan on or after December 27, 2020, then the grant received under the SVOG program is reduced by the PPP loan amount.

Grant amounts received under the SVOG program depend upon when the NFP began operations, as follows:

- *Eligible entities in operation on January 1, 2019:* The grant will be for an amount equal to the lesser of (a) 45 percent of the entity's 2019 gross earned revenue, or (b) $10 million.
- *Eligible entities that began operations after January 1, 2019:* The grant will be for an amount equal to the lesser of (a) the average monthly gross earned revenue for each full month the entity was in operation in 2019, multiplied by six, or (b) $10 million.

SVOG funds may be used to cover certain expenses, including payroll, rent, scheduled mortgage or debt payments, state and local taxes and fees, and other ordinary and necessary business expenses. Funds may not be used to buy real estate, make investments or loans, contribute to political causes, or remit payments on loans originating after February 15, 2020. An NFP that receives funds must comply with the recordkeeping requirements of the SVOG program.

The SVOG program is structured as a grant, not as a loan. Therefore, an NFP should apply the guidance in ASC 958-605 to funds received through the SVOG program, similar to the contribution model used to account for PPP funds. SVOG funds qualify as a conditional contribution, similar to PPP funds, so NFPs need to apply judgment to determine if qualifying expenses are incurred subject to federal uniform guidance in order to recognize contribution revenue as expenses are incurred.

3.6 Accounting for provider relief funds

The CARES Act created the PRF, which is administered by the U.S. Department of Health and Human Services, to reimburse eligible health care providers for health-care-related expenses and lost revenue attributable to COVID-19.

Because PRF payments are conditioned upon incurring health-care-related expense or lost revenue attributable to COVID-19, and because noncompliance with the terms and conditions would result in the return of the payment, the payments would be considered conditional contributions under ASC 958-605. NFPs that receive PRF monies should account for these funds pursuant to the guidance in ASC 958-605-25-13, which states that funds received under conditional grants should be recognized as a refundable advance, until the conditions have been substantially met or explicitly waived by the grantor.

ASC 958-605-25-13

A transfer of assets with a conditional promise to contribute them shall be accounted for as a refundable advance until the conditions have been substantially met or explicitly waived by the donor. Some entities transfer cash or other assets with both donor-imposed restrictions and stipulations that impose a condition on which a gift depends. If a restriction and a condition exist, the transfer shall be accounted for as a refundable advance until the condition on which it depends is substantially met. A transfer of assets after a conditional promise to give is made and before the conditions are met is the same as a transfer of assets with a conditional promise to contribute those assets. A change in the original conditions of the agreement between promisor and promisee shall not be implied without an explicit waiver (see paragraph 958-605-35-2).

NFPs should evaluate their individual facts and circumstances to determine whether conditions have been met or substantially met at the reporting date—that is, if the NFP believes it is probable that it meets all of the eligibility criteria for a PRF payment. In most instances, these payments would be classified as donor-restricted contributions. However, if an NFP elects the simultaneous release accounting policy option described in ASC 958-605-45-4A and 45-4B, which is for donor-restricted contributions whose restrictions are met within the same reporting period, then it would be permitted to report the contribution revenue directly in net assets without donor restrictions.

ASC 958-605-45-4A

An NFP may elect a policy to report donor-restricted contributions whose restrictions are met in the same reporting period as the revenue is recognized as support within net assets without donor restrictions provided that the NFP has a similar policy for reporting investment gains and income (see paragraph 958-220-45-24), reports consistently from period to period, and discloses its accounting policy.

ASC 958-605-45-4B

An NFP may elect the policy described in paragraph 958-605-45-4A for donor-restricted contributions that were initially conditional contributions (the condition has been met) without also having to elect it

for other donor-restricted contributions or investment gains and income provided that the NFP reports consistently from period to period and discloses its accounting policy.

3.7 Going concern considerations

NFPs are required to evaluate their ability to continue as a going concern within one year after the financial statements are either issued or made available to be issued under the guidance in ASC 205-40. If an NFP concludes that there is substantial doubt about its ability to continue as a going concern or that its plans alleviate that doubt, it must provide disclosures to that effect in the financial statements.

In addition, an NFP must evaluate whether its analysis sufficiently considers the impact of COVID-19 when determining whether substantial doubt exists about its ability to continue as a going concern for one year after the date of the financial statements or whether its plans alleviate substantial doubt.

Appendix A: Cited guidance

The following table contains the titles of guidance cited in this publication from both the FASB's Accounting Standards Codification (ASC) and relevant Accounting Standards Updates (ASUs).

Quick reference	Title
ASC 205-40	*Presentation of Financial Statements: Going Concern*
ASC 250	*Accounting Changes and Error Corrections*
ASC 270	*Interim Reporting*
ASC 321	*Investments – Equity Securities*
ASC 323	*Investments – Equity Method and Joint Ventures*
ASC 326-30	*Financial Instruments – Credit Losses: Available-for-Sale Debt Securities*
ASC 330	*Inventory*
ASC 350-20 ASC 350-40	*Intangibles – Goodwill and Other: Goodwill* *Intangibles – Goodwill and Other: Internal-Use Software*
ASC 360	*Property, Plant and Equipment*
ASC 405	*Liabilities*
ASC 470-50 ASC 470-60	*Debt: Modifications and Extinguishments* *Debt: Troubled Debt Restructurings by Debtors*
ASC 805	*Business Combinations*
ASC 820	*Fair Value Measurement*
ASC 840	*Leases*
ASC 842	*Leases*

ASC 848	*Reference Rate Reform*
ASC 958-205 ASC 958-605 ASC 958-805	*Not-for-Profit Entities: Presentation of Financial Statements* *Not-for-Profit Entities: Revenue Recognition* *Not-for-Profit Entities: Business Combinations*
ASU 2016-01	*Recognition and Measurement of Financial Assets and Financial Liabilities*
ASU 2016-02	*Leases (Topic 842)*
ASU 2016-13	*Measurement of Credit Losses on Financial Instruments*
ASU 2016-14	*Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*
ASU 2016-18	*Restricted Cash*
ASU 2018-08	*Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*
ASU 2018-13	*Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement*
ASU 2018-15	*Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*
ASU 2019-03	*Not-for-Profit Entities (Topic 958): Updating the Definition of* Collections
ASU 2020-04	*Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting*
ASU 2020-05	*Revenue from Contracts with Customers (Topic 606) and Leases (Topic 842): Effective Dates for Certain Entities*
ASU 2020-07	*Not-for-Profit Entities (Topic 958): Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets*
ASU 2021-01	*Reference Rate Reform (Topic 848): Scope*
ASU 2021-03	*Accounting Alternative for Evaluating Triggering Events*

Appendix B: Other acronyms

The following table features the complete names of government programs, legislation, and other quick references that were cited in this Viewpoint.

Quick references	Title/organization
CARES Act	*The Coronavirus Aid, Relief, and Economic Security Act*
FIFO	*First-in, first-out*
LIBOR	*London Interbank Offered Rate*
LIFO	*Last-in, first-out*
NAV	*Net asset value*
PCC	*Private Company Council*
PPP	*Paycheck Protection Program*
PRF	*Provider Relief Fund*
SBA	*Small Business Administration*
SVOG	*Shuttered Venue Operators Grant*
TDR	*Troubled debt restructuring*
UPMIFA	*Uniform Prudent Management of Institutional Funds Act*

Appendix C: Grant Thornton publications

The following contains the titles of Grant Thornton publications cited in this document.

Leases: Navigating the guidance in ASC 842
Snapshot 2020-15, “Accounting for rent concessions”
Snapshot 2021-06, “Accounting alternative for evaluating triggering events”
New Developments Summary 2016-11, “FASB amends NFP financial statement presentation”
New Developments Summary 2018-06, "FASB clarifies scope of contribution accounting"
New Developments Summary 2020-08, “Reference rate reform”

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