

FASB Accounting Update

Megan Herde Crane, CPA
Assurance Associate Director

DEANDORTON

Objectives

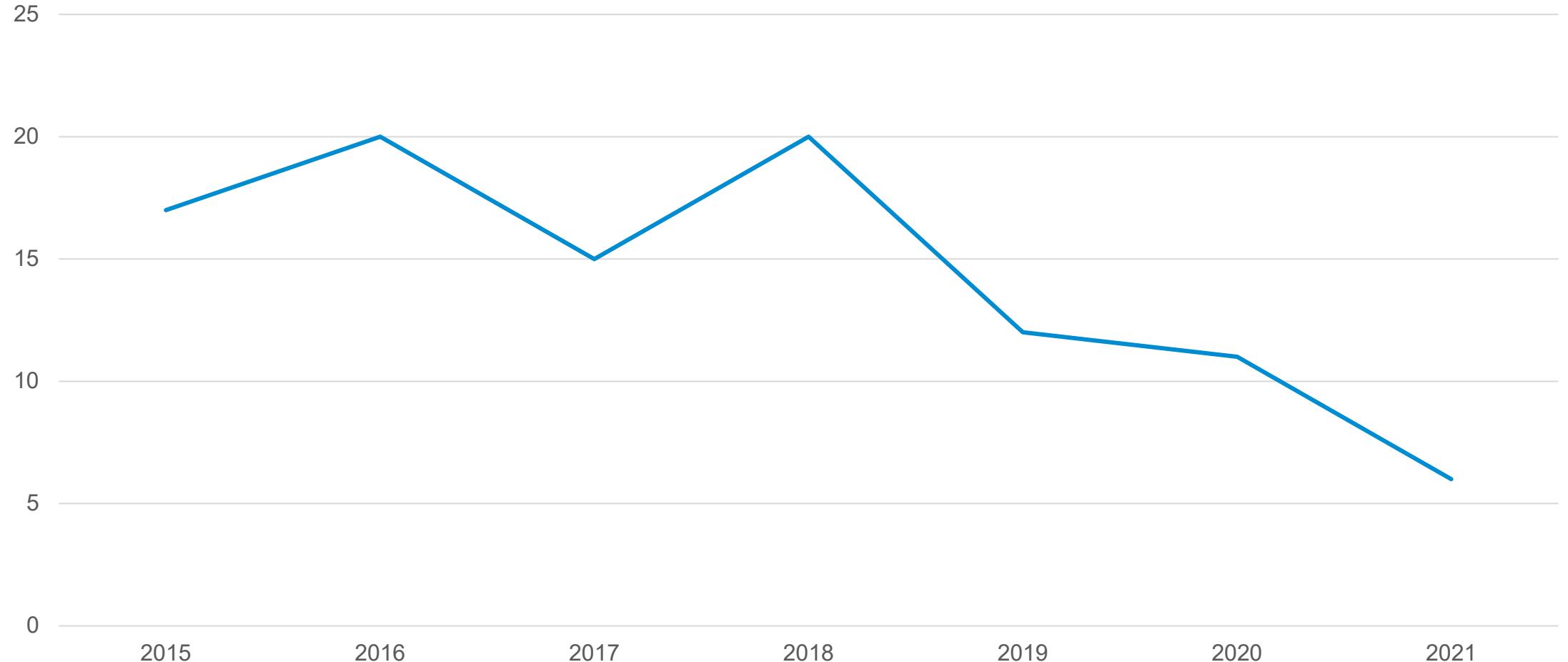
1. Discuss current trends
2. Overview of FASB pipeline and other matters
3. Gain an understanding of the new Accounting Standards Updates (ASUs)
4. Goodwill impairment triggering events
5. Define lease standards

Current Trends

Current trends in accounting and auditing

- Working remotely
- Technology
- Outsourcing
- Data analytics
- Reference rate reform
- Tracking Environmental, Social, and Governmental (ESG) metrics

New ASU trend



Through October 15, 2021

FASB projects (fasb.org)

- Conceptual and disclosure framework
- Inventory, interim reporting and income tax disclosures
- Intangibles and goodwill
- Consolidation
- Accounting for contingent consideration
- Segments
- Leases- use of risk free rate (asset class vs. entity wide)
- FASB post implementation reviews (CECL, Revenue, Leases)
- Current Expected Credit Losses (CECL) initial FASB review indicates:
 - Little impact on trade accounts receivable
 - Benefits
 - Homogenizing receivable write-off policy
 - Increasing controls around their customer credit risk analysis
 - Improving the classification of financial assets as trade receivables or financing receivables
 - Some discussion about excluding trade receivables for private companies

Accounting Standards Update

2021 ASUs

- ASU 2021-01: Reference Rate Reform
- ASU 2021-02: Revenue from Contracts with Customers (Practical Expedient)
 - Franchisors
- ASU 2021-03: Intangibles – Goodwill and Other: Accounting Alternative for Evaluating Triggering Events
- ASU 2021-04: Earnings Per Share, Debt Modifications and Extinguishments, Compensation – Stock Compensation, and Derivatives and Hedging – Contracts in Entity’s Own Equity

2021 ASUs

- ASU 2021-05: Leases (Topic 842): Lessors – Certain Leases with Variable Lease Payments
- ASU 2021-06: Presentation of Financial Statements (Topic 205), Financial Services – Depository and Lending (Topic 942) and Financial Services – Investment Companies (Topic 946)
- ASU 2021-07: Compensation – Stock Compensation (Topic 718): Determining the Current Price of an Underlying Share for Equity-Classified Share-Based Awards
- ASU 2021-08: Business Combinations (Topic 805)

2021 ASUs

- ASU 2021-09: Leases (Topic 842): Discount Rate for Lessees That are Not Public Business Entities
- ASU 2021-10: Government Assistance (Topic 832): Disclosures by Business Entities about Government Assistance

ASU 2021-01: Reference Rate Reform

- Scope
 - Contracts that reference LIBOR or an interest rate that has been discontinued or is anticipated to be discontinued
- Main provisions
 - Optional expedients and exceptions for applying GAAP to contracts, hedging relationships, and other transactions affected by reference rate reform if certain criteria are met
 - Continued application of hedge accounting for hedge relationships that are impacted by reference rate reform yet remain highly effective

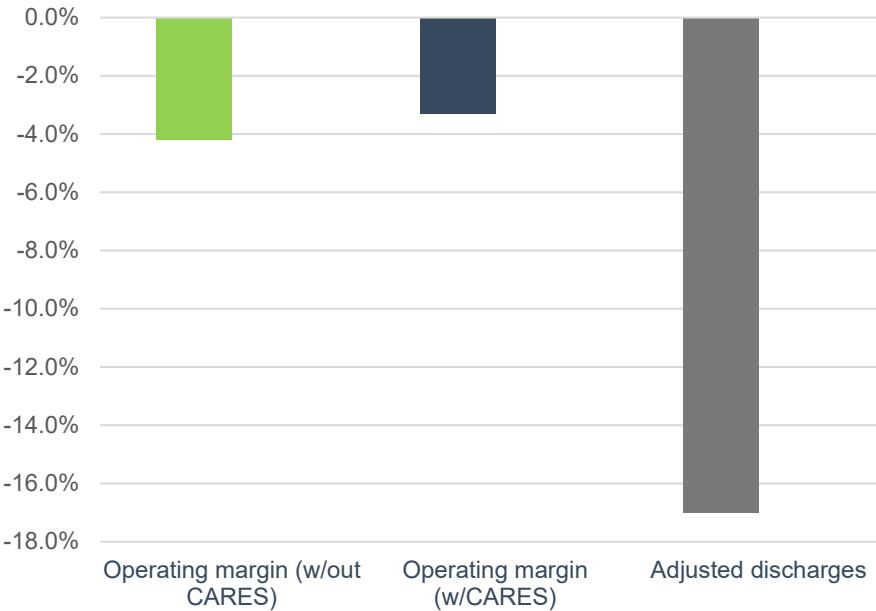
Goodwill Impairment

ASU 2021-03: Intangibles – Goodwill

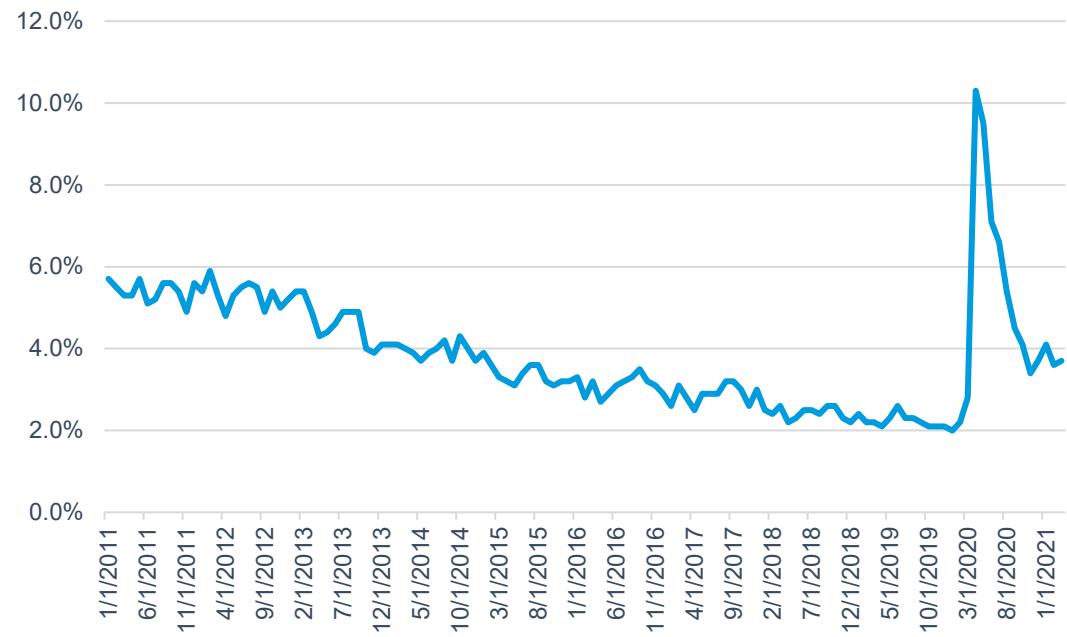
- Accounting alternative for evaluating triggering events
 - Private companies and not-for-profit entities
 - Removes need for an interim impairment assessment
 - Only required to perform impairment assessment at **end** of reporting period
 - Prospective basis post December 15, 2019

A year of triggering events

Median Change January and February
2021 from 2020



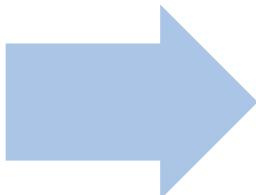
Health care unemployment rate



A year of triggering events

Triggering event

- External/market
 - Economy
 - Industry
 - Share price
- Internal
 - Cost
 - Cash flow



Goodwill impairment test

- Certain inputs and assumptions used in applying the methodologies may need to be revised from prior analyses

Goodwill impairment triggering event alternative

- Additional goodwill impairment alternative



Private companies and not-for-profit entities that only prepare financial statements compliant with U.S. generally accepted accounting principles (GAAP) on an annual basis



Private companies and not-for-profit entities that prepare GAAP-compliant financial statements in interim periods



Public companies

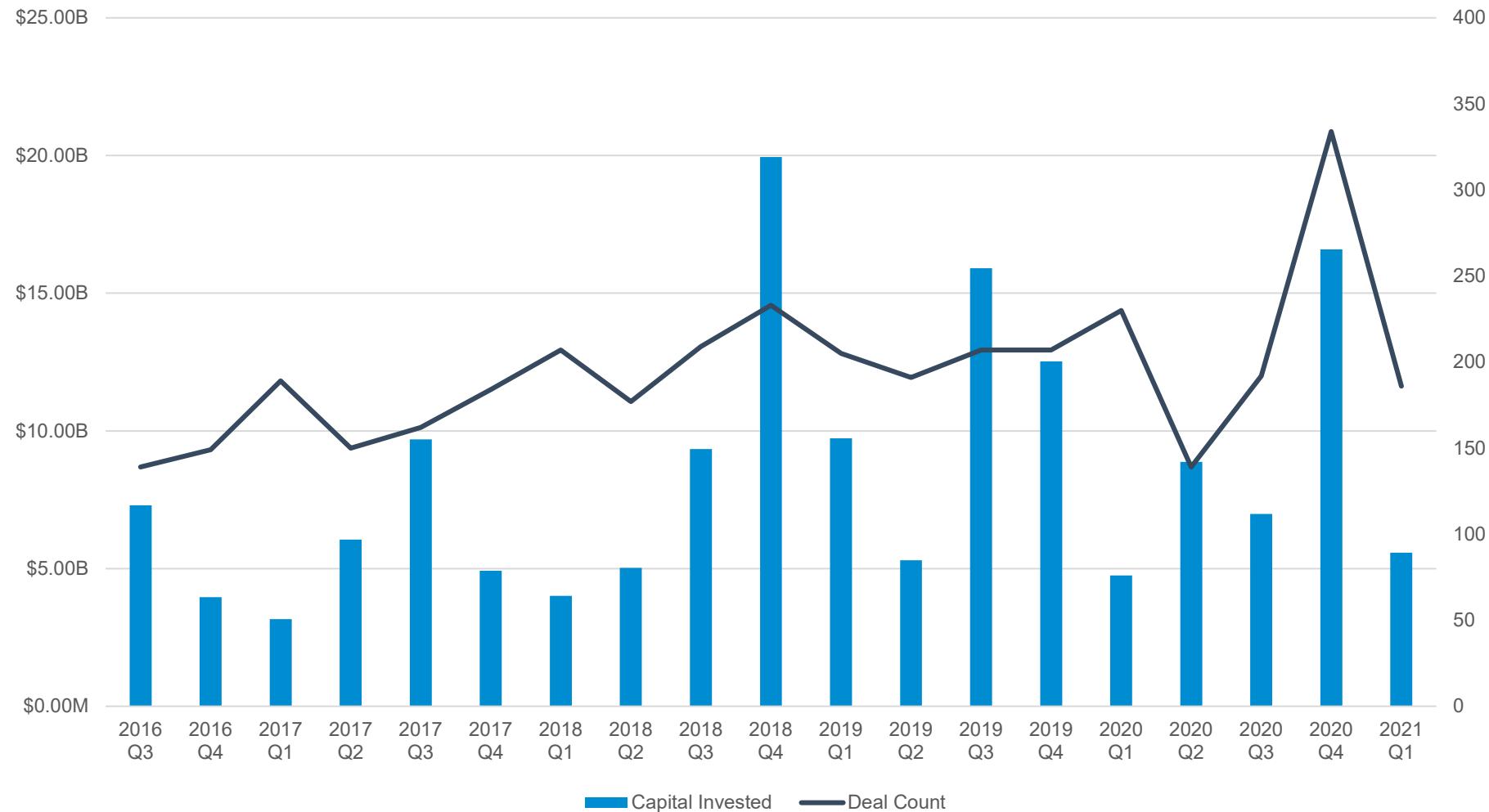
Goodwill impairment triggering event alternative

- Additional goodwill impairment alternative

Allow qualifying entities to perform any goodwill triggering event impairment test only on their annual reporting date (i.e., as of their year end), rather than at the triggering event date

Business Combinations

Healthcare transaction environment



Recent complexities in healthcare purchase accounting

- Purchase consideration
 - Contingent consideration more often material
 - Sellers' notes
 - Complex rollover arrangements
 - Apparent bargain purchases
- Intangible assets
 - Data
 - Developed technology
 - IPR&D

2021-08: Business Combinations

- In response to application of Topic 606 in a business combination
- Accounting for acquired revenue contracts with customers in a business combination
 - Require that an entity (acquirer) recognize and measure contract assets and contract liabilities acquired in a business combination in accordance with Topic 606
 - At the acquisition date, an acquirer should account for the related revenue contracts in accordance with Topic 606 as if it had originated the contracts

2021-08: Business Combinations

- Practical expedients available for acquirers
- Effective dates
 - Public fiscal year beginning after December 15, 2022
 - Private fiscal year beginning after December 15, 2023
 - Early adoption permitted

Leases

ASU No. 2016-02: Leases (Topic 842)

- Effective for year ends beginning after
 - December 15, 2018 (public)
 - A public business entity
 - A nonprofit entity has issued, or is a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market
 - December 15, 2021 (private)
- A June year-end would be July 1, 2022

Scope

- The new standard applies to all entities: public, private, and nonprofit, whether large or small
- It applies to all leases, including subleases, ***other than the following:***
 - Leases of intangible assets
 - Leases to explore for or use minerals, oil, natural gas, and similar nonregenerative resources
 - Leases of biological assets, including timber
 - Leases of inventory
 - Leases of assets under construction
- Don't forget potential leases embedded within other types of agreements

Key changes

- Definition of a lease
- All leases* to be on the balance sheet
 - Capital lease  financing lease
 - Operating lease  operating lease

**With lease terms of more than 12 months*

Definition of a lease

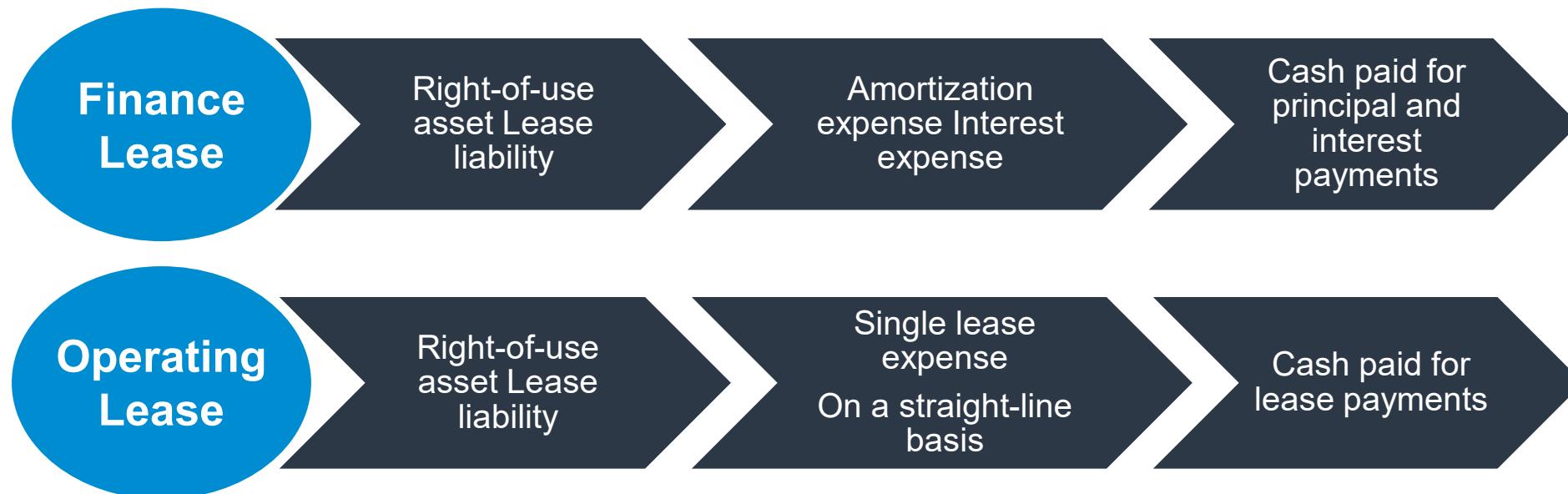
FASB ASC 840	FASB ASC 842
An agreement conveying the right to use property, plant, or equipment (land and/or depreciable assets) usually for a stated period of time	A contract, or part of a contract, that conveys the right to control the use of identified property, plant, or equipment (an identified asset) for a period of time in exchange for consideration

Financing leases

- When a lease meets any of the following specified criteria at commencement, the lease should be classified as a **financing lease** by the lessee and as a sales-type lease by the lessor
- These criteria can be summarized as follows:
 - The lease transfers ownership to the lessee
 - The purchase option is reasonably certain to be exercised
 - The lease term is for the major portion of the asset's remaining economic life
 - The present value of lease payments and the residual value exceeds substantially all the fair value of the underlying asset
 - The specialized nature of the underlying asset results in no expectation of alternative use after the lease term

Leases

- Lessee accounting



Implications

- Key metrics and debt covenants

Metric	Effect
Current ratio (current assets/current liabilities)	Decrease
Leverage ratio (debt/equity)	Increase
Return on assets (net income/assets)	Decrease
Debt to Earnings Before Interest, Taxes, Depreciation, and Amortization (debt/EBITDA)	Increase

Lease accounting lessons

- Get an early start on compiling lease inventory including embedded leases
 - Remember a lease requires exclusive control over an identified asset
- Identifying the proper incremental borrowing rate (IBR) can be challenging
- Private companies – strongly consider practical expedient to use the risk free rate for IBR

Interest Rate (2021-09)

- Topic 842: practical expedient to use risk-free rate for all leases for non public entities
- ASU 2021-09:
 - Lessees can elect the risk-free rate by class of underlying asset, unless the rate implicit in the lease is readily determinable for any individual lease

Lease accounting lessons

- Take advantage of practical expedients
- Renewals are now accounted for if “reasonably certain” to extend
- Tools are available
 - Excel, compliance software (e.g. Visual Lease), lease management software

Allocation of consideration in the contract

- If multiple leased assets are controlled by a single contract, you might need to allocate the contract price between the assets
- Lease vs. non-lease components
 - If a lease includes leased assets as well as service components, you will allocate between the components
 - Practical expedient
 - You can make a policy election to include service components with the lease component
 - Must apply across the board

ASU 2021-05: Leases

- Lessors: certain leases with variable lease payments
 - Variable lease payments do not depend on reference index or rate and
 - Would have resulted in selling loss at lease commencement if classified as sales-type or direct financing
 - Classify as an operating lease
 - Fiscal years post December 15, 2021 for public and fiscal years post December 15, 2022 for private

Healthcare specific nuances

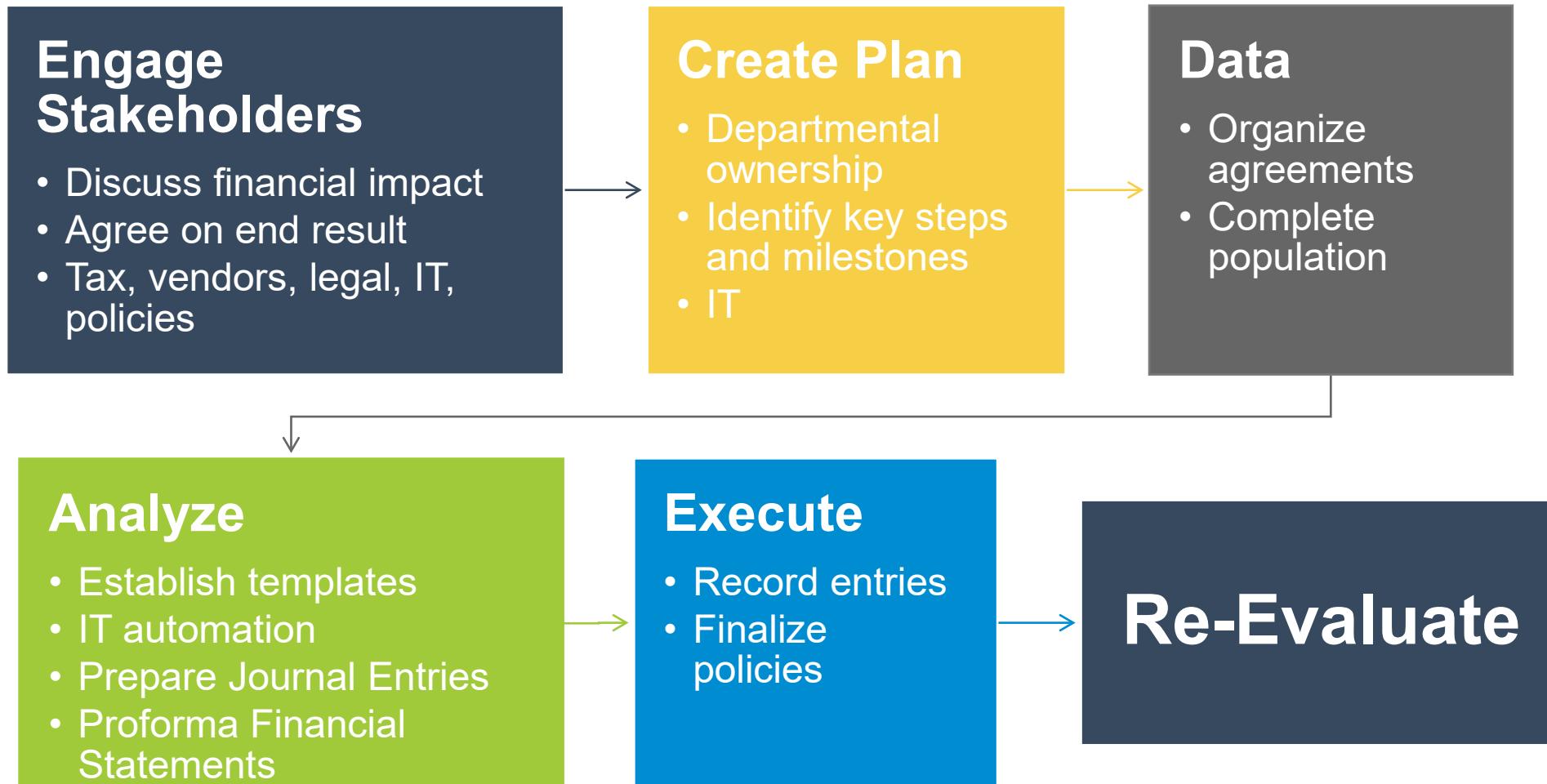
- Consumable contracts with “free equipment” associated with purchases
- Drug manufacturer contracts with “free equipment”
- Lab contracts
- Building leases
- Vehicles
- Technology equipment

Lease accounting software

Characteristics	Vendor Partners					
	Self-Service		Smaller Lease Portfolio	Medium-Sized Portfolio	Larger Lease Portfolio	
Vendor Name	RSM Lease Accounting Software	Compliance Tool Kit	LeaseQuery	NetLease	Visual Lease	Tango
Overview	<ul style="list-style-type: none"> Simple and secure way to account for leases Has ASC 842/ IFRS 16 functionality 	<ul style="list-style-type: none"> Preconfigured database with short implementation timeline Has ASC 842/ IFRS 16/ GASB 87 functionality 	<ul style="list-style-type: none"> Built by accountants for accountants Has ASC 842/ IFRS 16/ GASB 87 functionality 	<ul style="list-style-type: none"> Built for NetSuite (Verified Native SuiteApp) Has ASC 842/ IFRS 16 functionality 	<ul style="list-style-type: none"> Over 20 years of experience in real estate lease management Has ASC 842/ IFRS 16/ GASB 87 functionality 	<ul style="list-style-type: none"> Over 20 years of experience in real estate lease management Has ASC 842/ IFRS 16 functionality Used by some of the largest retail and restaurant companies
Sweet Spot	<= 20 leases	< 200 leases	20 to 200 leases	NetSuite ERP	>200 leases	Large national chains looking for highly customizable solution
First Look	<ul style="list-style-type: none"> Lowest cost option For small portfolios only Accounting only compliance 	<ul style="list-style-type: none"> Condensed timeline Accounting only compliance 	<ul style="list-style-type: none"> Accounting only compliance 	<ul style="list-style-type: none"> NetSuite ERP Both Lessee and Lessor Accounting 	<ul style="list-style-type: none"> Strong reporting functionality for compliance and for Ad Hoc Report creation 	<ul style="list-style-type: none"> Large retail / restaurant / real estate clients
Strengths	<ul style="list-style-type: none"> User friendly and pre-configured Lower cost software and implementation Can upgrade to LeaseQuery 	<ul style="list-style-type: none"> User friendly and pre-configured Option to optimize at a later point Lower implementation cost option Strong standard reports (e.g. disclosure, rollforward) 	<ul style="list-style-type: none"> User-friendly interface Strong accounting capabilities to achieve compliance 	<ul style="list-style-type: none"> No integration builds/ quick implementations Looks and operates the exact same way as NetSuite Fully supports lessor accounting 	<ul style="list-style-type: none"> User-friendly and easy to configure Flexible for configuration updates after Go-Live Ability to import most modifications, terminations, and impairments Strong standard reports (e.g. disclosure, rollforward) 	<ul style="list-style-type: none"> Excellent user interface Visual dashboard for management insight Ability to manage and account for complex real estate leases Part of broader Integrated Workplace Management Solution
Outsourcing Option	No	No	Yes	Yes	Yes	Yes
How it's priced	<ul style="list-style-type: none"> Tiered based on the number of lease records (\$500 to \$2,000/ yr.) Free trial for first two leases entered 	<ul style="list-style-type: none"> Tiered based on the mix of real estate and equipment records (assets) Minimum: \$10,000/yr. 	<ul style="list-style-type: none"> \$84/per record (asset) Minimum: \$8,400/yr. + implementation services 	<ul style="list-style-type: none"> Tiered based on the number of records (assets) No minimum, starts at \$7,000/yr. for 30 records 	<ul style="list-style-type: none"> Tiered based on the mix of real estate and equipment records (assets) Minimum: \$12,500/yr. 	<ul style="list-style-type: none"> 2 Pricing Models: <ul style="list-style-type: none"> Tiered based on greater of Revenue or Location Count Variable based on number of leases- starting at \$15,000/yr. for up to 100 leases

Note: Assumes 50/50 split between real estate & equipment leases

Implementation



Additional information

- International Financial Reporting Standards
 - All finance leases
 - Implementation date January 1, 2019
- Governmental Accounting
 - Single model
 - Retroactive
 - FY22
- Software providers
 - Tangoanalytics.com
 - AMTdirect.com
 - Costarmanager.com
 - Leasequery.com

Disclosures prior to adoption

- Assessment team
- Education and guidance to business units
- Compiled current population of leases and updating
- Developing internal controls
- Monitoring FASB activity and various non-authoritative groups

Lease disclosures

- A *lessee* shall disclose all of the following:
 - Description of leases
 - Basis, terms, and conditions of any variable payments
 - Options to extend
 - Residual value guarantees
 - Covenants
 - Maturity analysis

Lease disclosures

- Finance leases
 - These leases mainly consist of (equipment, vehicles, etc.) for the use of (operations, deliveries, etc.)
 - Termination of the leases generally are prohibited unless there is a violation under the lease agreement

Lease disclosures

- Operating leases
 - The Company leases office space for the branch sales offices that expire in various years through [20x5]
 - These leases generally contain renewal options for periods ranging from [1] to [12] years and require the Company to pay all executory costs (property taxes, maintenance, and insurance)
 - Lease payments have an escalating fee schedule, which range from a [1] to [5]% increase each year
 - Termination of the leases is generally prohibited unless there is a violation under the lease agreement
 - A portion of the leased space is subleased under leases expiring over the next [3] years

Lease disclosures

- **Short-Term Leases**
 - The Company leases certain equipment on a seasonal demand basis
 - The Company has elected the practical expedient for these short-term equipment leases as the lease terms are less than 12 months
 - 22 total short-term lease are in place as of December 31, 20x1, expense relating to these agreements of \$[] and \$[] is included in operating expenses for the years ending December 31, 20X1 and 20X0, respectively
- **All Leases**
 - The Company has no material related-party leases
 - The Company's lease agreements do not contain any material residual value guarantees or material restrictive covenants

Leases and your audit

“We don’t have any leases.”

“We are so busy, we will work on that later.”

“We can track that in Excel.”

“Our leases aren’t material.”

“We have several leases, but they are not material.”

“Our leases are all short-term.”

Leases and your audit

- Involve your auditor early
 - What is your organization's plan?
 - Who is executing the plan?
- Timing of testing implementation
- What is your auditable evidence of your population?
- Preparing and understanding your disclosures

FASB lease roundtables (Sept. 18, 2020)

- Rate implicit in lease – see 2021-09
- Incremental borrowing rate (collateralized asset)
- Embedded leases
- Lease modifications
- Lease allocation of fixed and variable payments
- *Private company council*
 - **Lessen any disclosure items?**
- *Materiality application*

A group of four professionals are gathered around a table in an office. A man in a blue shirt is on the left, looking towards a woman with blonde hair in the center. In the center, a man with a beard and glasses is looking at a laptop screen. On the right, a woman with curly hair is pointing towards the laptop. They are all looking at the screen together. The background shows a bookshelf with books and some decorative items.

Questions?

DEANDORTON

Thank you

Megan Herde Crane, CPA

Assurance Associate Director

mcrane@deandorton.com

859.425.7643