Coronavirus: Financial reporting considerations

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TABLE OF CONTENTS

Introduction .......................................................................................................................... 1
Overall impact to the financial statements ................................................................. 1
Asset impairment .............................................................................................................. 1
   Equity securities ........................................................................................................ 1
   Equity method investments ....................................................................................... 1
Debt securities, prior to the adoption of ASU 2016-13, Financial Instruments –  
   Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments .................................................................................................................. 2
Debt securities, subsequent to the adoption of ASU 2016-13...................................... 2
Loans and other receivables, prior to the adoption of ASU 2016-13............................ 3
Loans and other receivables, subsequent to the adoption of ASU 2016-13.................. 3
Inventories ...................................................................................................................... 3
Goodwill ......................................................................................................................... 4
Indefinite-lived intangible assets ................................................................................... 4
Long-lived assets to be held and used .......................................................................... 4
Fair value ....................................................................................................................... 4
Sales of HTM debt securities ......................................................................................... 5
Lease considerations ..................................................................................................... 5
   Impairment .............................................................................................................. 5
   Operating lease receivables under ASC 842 ........................................................... 5
   Lease concessions .................................................................................................. 5
Loan and debt modifications and classification ......................................................... 7
   Classification by debtor ........................................................................................ 7
   Modifications: Debtor accounting ...................................................................... 7
   Modifications: Lender accounting .................................................................... 7
Business interruption insurance considerations ....................................................... 8
Obligations for exit or disposal costs and contingencies ............................................. 8
Revenue recognition .................................................................................................... 8
   Variable consideration ....................................................................................... 8
   Contract modifications ...................................................................................... 9
   Collectibility ....................................................................................................... 9
   Revenue recognition over time ...................................................................... 9
Hedge accounting and derivative valuation ............................................................... 10
Stock compensation .................................................................................................... 11
Tax considerations
Consolidation
Paycheck Protection Program loans and other government assistance
Paycheck Protection Program loans
  Borrower accounting
  Lender accounting
Other government assistance
Going concern, risks and uncertainties
Certain SEC and regulatory reporting considerations
GASB activities and resources
Ongoing developments
Introduction

The effects of the coronavirus are evolving rapidly and are unique for each entity’s circumstances. In addition to addressing the serious operational impacts of the coronavirus, it is important that all entities consider how the coronavirus affects their financial reporting. We offer the following overview of several matters for consideration during this critical time.

Overall impact to the financial statements

Financial statements need to reflect all material current and potential effects of the coronavirus that existed at the period-end date. Subtopic 225-20, “Income Statement – Unusual or Infrequently Occurring Items,” of the Financial Accounting Standards Board’s (FASB) Accounting Standards Codification (ASC) addresses unusual or infrequently occurring items, such as this worldwide pandemic, and requires such items to be included in income from continuing operations, and where separately identifiable and directly related as a separate line item. In addition, the footnotes should be supplemented with disclosure as necessary to convey the nature and financial effects of each event or transaction.

The significant deterioration in economic conditions associated with the coronavirus is generally viewed to have begun in the first quarter of 2020 and is, therefore, largely expected to be disclosed as a nonrecognized subsequent event for calendar-year-end entities that have not yet finalized their 2019 financial statements. Accordingly, consideration should be given to disclosure of subsequent events in accordance with ASC 855, “Subsequent Events.”

The situation will continue to evolve such that, at each reporting period end, consideration should be given to subsequent events and distinguishing between those that should be recognized versus unrecognized under the provisions of ASC 855. In other words, for entities with year ends in 2020 (e.g., January, February, March) and for quarterly financial reporting in 2020, entities will need to give more specific consideration to the date events related to the pandemic occurred and the effect of this on recognition and disclosure in the financial statements.

Asset impairment

As a consequence of the significant deterioration in economic conditions associated with the coronavirus pandemic, careful consideration should be given to both financial and nonfinancial assets and the need to recognize impairment losses or increased allowances for credit losses (as required by the relevant accounting guidance). A high level overview of the accounting guidance by asset type is discussed in the remainder of this section.

Many of the sections that follow discuss investment impairment or collectibility issues related to certain financial assets.

Equity securities

Upon the adoption of FASB Accounting Standards Update (ASU) 2016-01, Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities, equity securities that are not subsequently measured at fair value through earnings are written down to fair value in accordance with ASC 321-10-35-3 if a qualitative assessment indicates that the investment is impaired and the fair value of the investment is less than its carrying value. We believe in many cases a qualitative assessment performed under current conditions will result in a conclusion that the investment is impaired, in which case management will need to determine the fair value of the investment to quantify the impairment loss. No consideration can be given to the fact that this impairment may be of short duration, and unlike the preexisting guidance discussed next, no consideration is given to whether the holder has the intent and ability to hold the security until it recovers.

Under the guidance in ASC 320-10-35 that was relevant to equity securities prior to the adoption of ASU 2016-01, consideration was given to the duration of the impairment, and only impairment that was
deemed to be *other than temporary* was required to be recognized. Additionally, impairment was recognized if the holder did not have the intent and ability to retain the equity investment for a sufficient period of time to allow for an anticipated recovery in fair value.

**Equity method investments**

For equity method investments, ASC 323-10-35-31 to 35-32A is the relevant impairment guidance to consider and requires loss recognition for losses in value that are other than temporary. This guidance mentions a series of operating losses of an investee, the absence of an ability to recover the carrying amount of the investment, or inability of the investee to sustain an earnings capacity that would justify the carrying amount of the investment as examples of some (but not all) factors to consider in making this determination.

**Debt securities, prior to the adoption of ASU 2016-13, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments**

ASC 320-10-35 is the relevant guidance to consider when recognizing impairment or expected credit losses on debt securities that are not accounted for at fair value through earnings. Under ASC 320-10-35, impairment losses are recognized on individual debt securities that have a fair value that is less than their amortized cost basis if, as of the balance-sheet date, management has the intent to sell the security or more likely than not will be required to sell the security before the recovery of its amortized cost basis. Thus, careful consideration should be given to upcoming cash needs in this challenging economic environment when performing this analysis. (Refer also to the separate section that follows on sales of held-to-maturity [HTM] debt securities.) Additionally, expected credit losses are recognized on individual impaired debt securities if management does not expect to fully recover the amortized cost basis. Changes in credit ratings and adverse conditions are two of numerous factors noted in ASC 320-10-35-33F that should be considered when estimating whether a credit loss exists. Entities should be mindful that credit ratings on individual securities may not be up to date and reflective of current conditions.

**Debt securities, subsequent to the adoption of ASU 2016-13**

Refer to [Temporary CECL relief for certain insured depository institutions](#) for an optional deferral certain institutions may elect.


- **HTM debt securities:** Under ASC 326-20, HTM debt securities and other investments carried at amortized cost (e.g., cash equivalents) are required to be evaluated on a collective basis with other assets within the scope of ASC 326-20 that have similar risk characteristics, when such other assets exist. Additionally, expected credit losses need to be recognized through an allowance for credit losses regardless of the relationship of the fair value of a security to its amortized cost basis. Refer to the additional discussion of the adoption of ASC 326-20 that follows in the context of loans and other receivables. The estimate of expected credit losses should include a measure for the expected risk of loss even if that risk is remote. As a consequence of this, the expectation is that circumstances in which an HTM security does not have an allowance for expected credit losses would be rare (e.g., securities of the U.S. government or its agencies). The concepts of *other than temporary* and the *intent or potential requirement to sell an HTM security* are no longer relevant to the consideration and recognition of expected credit losses.

- **AFS debt securities:** Under ASC 326-30, AFS debt securities continue to be evaluated for impairment individually. Credit losses are recognized on individual securities that have a fair value less than amortized cost through an allowance rather than as a direct write-down to the amortized cost basis of
the security, unless the *intent or more-likely-than not* requirement to sell exists. In determining whether a credit loss exists, consideration should no longer be given to the length of time the security has been impaired or to recoveries or additional declines in the fair value after the balance-sheet date. The concept of *other than temporary* is no longer relevant, and in light of current conditions, it will be more difficult to conclude qualitatively that credit losses are not present in an impaired AFS debt security, which will trigger the need for projecting expected cash flows to quantify and recognize expected credit losses.

**Loans and other receivables, prior to the adoption of ASU 2016-13**

ASC 310-10-35 is the primary guidance to consider in recognizing impairment and an allowance for expected losses on loans, commitments to lend and other receivables. Under its provisions, incurred losses are recognized. Consideration typically is given to historical loss rates when estimating the period-end allowance, with adjustments made to the historical loss rates as necessary so that the loss rates on which the allowance is based are reflective of current conditions. These adjustments are particularly important in light of the current severe and dramatically different economic conditions.

**Loans and other receivables, subsequent to the adoption of ASU 2016-13**

Refer to [Temporary CECL relief for certain insured depository institutions](#) for an optional deferral certain institutions may elect.

ASC 326-20 is the relevant guidance to consider when recognizing expected credit losses on financial assets measured at amortized cost, including loans, other receivables, contract assets and cash equivalents. It also applies to net investments in leases, reinsurance receivables and off-balance-sheet credit exposures. As noted in a preceding section, ASC 326-20 requires assets within its scope to be evaluated on a collective basis with assets that have similar risk characteristics. The estimate of expected credit losses should include a measure for the expected risk of loss even if that risk is remote. As a consequence of this, the expectation is that circumstances in which an asset that is within its scope does not have an allowance for expected credit losses would be rare. Amongst other changes, ASC 326-20 requires life of asset expected, rather than incurred, losses to be recognized and consideration to be given to current conditions, as well as reasonable and supportable forecasts.

The significant deterioration in current conditions related to the coronavirus pandemic began in the latter half of the first quarter of 2020. As such, we generally do not believe it would be appropriate for entities adopting ASU 2016-13 as of January 1, 2020 to use hindsight and adjust their opening allowance for credit losses for this deterioration. Rather, these deteriorated conditions should be reflected when recognizing expected credit losses in the first quarter of 2020. In applying the provisions of ASC 326-20-30-6, consideration is given to troubled debt restructurings (TDRs) that the reporting entity (creditor) reasonably expects it will execute. This aspect of ASC 326-20 is likely to become particularly relevant in the current environment given the expectation that there will be a dramatic increase in loan modifications and that some of those modifications will be TDRs. Refer to the discussion of loan modifications that follows.

**Inventories**

We expect inventory production to be at severely diminished levels for certain entities as a consequence of forced business closures, reduced demand and other ramifications of the coronavirus pandemic. ASC 330-10-30-3 indicates that the amount of fixed overhead allocated to each unit of production should not be increased as a consequence of abnormally low production or idle plants. In other words, unallocated costs need to be expensed as incurred.

Additionally, ASC 330-10-35 addresses the subsequent measurement of inventory and requires losses to be recognized when the net realizable value of the inventory, or in some cases, the utility of the goods, is less than cost. In addition, losses are required to be recognized in a similar manner on firm purchase commitments related to goods for inventory. Reduced demand for oil that is attributable to the coronavirus...
pandemic and the resultant significant declines in oil prices is just one example of a type of inventory for which loss recognition may be warranted.

**Goodwill**

Repercussions of the coronavirus pandemic could affect estimates of future cash flows and earnings, thereby materially affecting the measurement of fair value of a reporting unit and resulting in the need to perform an interim impairment test of goodwill. The unit of account when testing goodwill for impairment is the reporting unit (in cases in which the relevant private company accounting alternative has not been elected), which is an operating segment or one level below an operating segment. ASC 350-20-35-30 states, "Goodwill of a reporting unit shall be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount." Examples of such events or circumstances (i.e., triggering events) are discussed in our article, *Interim goodwill impairment testing by SEC filers*.

If these triggering events or other relevant events occurred, entities must consider to what extent they (along with any offsetting positive and mitigating events and circumstances) impact the fair value and carrying amount of their reporting units in order to determine whether interim impairment testing is required. This consideration is based on whether these events collectively cause it to be more likely than not that the fair value of a reporting unit is less than its carrying amount. Even private companies that have elected to amortize goodwill on a straight-line basis are required to test for impairment when a triggering event occurs indicating the fair value of the entity (or reporting unit) may be below its carrying amount.

**Indefinite-lived intangible assets**

Like goodwill, an indefinite-lived intangible asset is required to be tested for impairment annually and more frequently if events or changes in circumstances indicate that it is more likely than not that the asset is impaired. The unit of account when testing indefinite-lived intangible assets for impairment is generally the asset itself. Triggering events similar to those relevant for goodwill would have to be considered in relation to the indefinite-lived intangible asset to determine whether interim impairment testing is required.

**Long-lived assets to be held and used**

These assets include those within the scope of ASC 360-10-15, such as property, plant and equipment. The unit of account when testing long-lived assets to be held and used for impairment is the asset group, which represents the lowest level for which identifiable cash flows are largely independent of the cash flows of other groups of assets and liabilities. An asset group almost always includes multiple assets. ASC 360-10-35-21 states, “A long-lived asset (asset group) shall be tested for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable.” The guidance lists examples of such events or changes in circumstances, including a significant decrease in the market price of a long-lived asset (asset group) and a significant adverse change in the business climate that could affect the value, among many others. If impairment testing is required at the same time as goodwill and (or) indefinite-lived intangible assets, the testing of indefinite-lived intangible assets must occur first, followed by long-lived assets to be held and used, with goodwill tested last. For further discussion, see our whitepapers, *Snapshot: Accounting for impairment of goodwill and other long-lived assets* and *Impairment testing of long-lived assets classified as held and used*.

**Fair value**

ASC 820, "Fair Value Measurement," indicates the objective of a fair value measurement is to determine the price at which an orderly transaction would take place between market participants under the market conditions that existed at the measurement date. While the effects of the coronavirus pandemic are causing market volatility, it would not be appropriate to disregard market prices at the measurement date, unless those prices are from transactions that are not orderly. ASC 820-10-35-54I and 35-54J contain useful guidance for identifying transactions that are not orderly.
Sales of HTM debt securities

Entities that are considering liquidating or transferring debt securities designated as HTM for upcoming cash needs or other reasons are advised to give consideration to the changes in circumstances that are outlined in ASC 320-10-25 as being consistent (versus inconsistent) with HTM classification. As noted in ASC 320-10-35-8 and 35-9, any sale or transfer of an HTM security that represents a material contradiction with the entity’s stated intent, or a pattern of such sales occurring, will trigger a requirement to transfer any remaining HTM securities to AFS. An example of a change in circumstances that is consistent with HTM classification is a sale or transfer due to significant deterioration in the issuer’s creditworthiness. As noted at ASC 320-10-25-4 and 25-5, a sale in advance of deterioration in the creditworthiness of the issuer (e.g., sales based solely on industry statistics), as well as sales due to events such as liquidity needs and changes in market interest rates, are not consistent with HTM classification. ASC 320-10-25-9 indicates that certain sales or transfers that are caused by an event that could not have been reasonably anticipated will not necessarily call into question the entity’s intent to hold other debt securities to maturity if the event is isolated, nonrecurring and unusual for the reporting entity.

In light of the subjectivity inherent in determining what sales or transfers of HTM securities are consistent with classification as HTM, entities should give careful consideration to the guidance in ASC 320-10, “Investments—Debt and Equity Securities—Overall,” and its specific facts and circumstances before undertaking a sale or transfer that could taint the ability to maintain or use the HTM designation for other debt securities.

Lease considerations

Impairment

Right-of-use (ROU) assets recognized by lessees under ASC 842, “Leases,” are subject to the impairment guidance in ASC 360-10-35. ROU assets might become impaired as a result of business closures or reduced usage, among other things. Any ROU asset that becomes impaired should subsequently be measured at its post-impairment carrying amount less accumulated amortization. After the impairment, amortization of the ROU asset generally would be recognized on a straight-line basis (unless another basis is more representative of the pattern in which the lessee expects to consume the remaining economic benefits from its right to use the underlying asset).

For lessors, under both ASC 840, “Leases,” and ASC 842:

- The guidance in ASC 310-10-35 prior to the adoption of ASU 2016-13 and ASC 326-20 after its adoption should be used to assess the potential impairment of net investments in sales-type leases and direct financing leases.

- Consideration should be given to the preceding discussion on long-lived assets for potential impairment recognition on the underlying assets.

Operating lease receivables under ASC 842

For lessors that have adopted ASC 842, if the collectibility of lease payments is assessed as probable at the commencement of an operating lease, and the collectibility assessment subsequently changes, the lessor should apply the guidance in ASC 842-30-25-13. Using that guidance, the lessor should recognize a current-period adjustment to income for any difference between: (a) the sum of (1) the lease income that would have been recognized based on straight-line recognition of lease payments and (2) variable lease payments recognized as income in the period in which the changes in facts and circumstances occur and (b) the amounts that have been collected from the lessee to date.

Lease concessions

A number of lessees are experiencing reduced cash flow as a result of the pandemic. Many lessors are providing economic relief in the form of lease concessions to their lessees, either voluntarily or as a result
of contractual obligations. The FASB staff Q&A, *Topic 842 and Topic 840: Accounting for Lease Concessions Related to the Effects of the COVID-19 Pandemic*, addresses whether lease concessions granted by lessors as a result of the coronavirus pandemic are required to be accounted for in accordance with the lease modification guidance in ASC 840 or 842 (as applicable).

The FASB staff guidance indicates that both lessees and lessors may elect to not apply the modification accounting guidance in ASC 840 and 842 to lease concessions granted as a result of the coronavirus pandemic, thereby eliminating the need to determine whether the terms of the lease explicitly provide for the possibility of such concessions. This election would only be permitted if the lease concessions result in the lease’s total cash flows being substantially the same as or less than the lease’s total cash flows prior to the concessions.

When a lessee or lessor elects to not apply the modification accounting guidance in ASC 840 and 842 to lease concessions resulting from the coronavirus pandemic, the accounting applied to the concessions depends on whether they only affect the timing of the payments (i.e., the concessions only defer payments without making any substantive changes to the total lease payments). When only the timing of payments is affected by the lease concessions, the FASB staff acknowledges that multiple accounting methods may be applied in practice, none of which it believes would be preferable to the others. The two specific accounting methods discussed by the FASB staff would result in the deferred payments resulting from the lease concessions being accounted for as either:

- Increases to lessors’ lease receivables and lessees’ payables as the receivables and payables accrue, respectively. (Under this method, both lessors and lessees continue to recognize income and expense, respectively, as they otherwise would. This method accounts for the concessions as if no changes were made to the lease.)

- Variable lease payments by both lessees and lessors.

When a lessee or lessor elects to not apply the modification accounting guidance in ASC 840 and 842 to lease concessions resulting from the coronavirus pandemic, and more than just the timing of the payments is affected by the lease concessions, the accounting for the concessions depends on the facts and circumstances. For example, if a lease concession results in a lease payment being forgiven or waived, it should be accounted for as a variable lease payment.

When a lessee or lessor decides to apply (rather than elect out of) the modification accounting guidance in ASC 840 and 842 to lease concessions resulting from the coronavirus pandemic, if the terms of the lease explicitly provide for the possibility of lease concessions resulting from the coronavirus pandemic, the concessions are accounted for as variable lease payments. If the terms of the lease do not provide for the possibility of such concessions, the concessions are accounted for using the modification guidance. For an entity that has adopted ASC 842, the modification provisions of ASC 842 apply, and a lessor and lessee should apply the guidance in ASC 842-10-25-8 to 25-18 to determine whether the modification should be accounted for as a separate contract or as a change to the existing contract. If ASC 842 has not been adopted, lessors and lessees must determine whether a new lease has been created, and if so, the accounting for any such new lease. This determination requires two tests. The first test determines whether the classification of the lease would have been different if the new terms had been in place at lease inception. If the classification would have been different, a new agreement is considered to have been created, and the second test is performed and determines the classification of the revised lease, as of the date of the revision in the lease terms. If the first test does not result in a new agreement, adjustments are made to the existing asset and obligation balances for any difference between the present value of the future minimum lease payments (calculated using the revised lease terms) and the outstanding obligation balance.

Based on the FASB staff guidance, the election to not apply the modification accounting guidance in ASC 840 and 842 to lease concessions granted as a result of the coronavirus pandemic should be made
consistently for leases with similar characteristics and in similar circumstances. In other words, the election may be made on a portfolio-by-portfolio basis.

The FASB staff also indicated in their guidance that disclosures about material concessions and their accounting effects should be provided by both lessors and lessees.

**Loan and debt modifications and classification**

If the impact of the coronavirus causes disruptions that result in cash flow problems, entities may need to amend terms of existing debt agreements or obtain waivers for debt covenant violations.

**Classification by debtor**

If there has been a covenant violation or other default at the balance-sheet date, debtors should consider whether the classification of long-term debt needs to be revised in accordance with ASC 470-10-45. Additional information about debt classification matters, including examples in which the borrower has violated a debt covenant at the balance-sheet date, can be found in our white paper, *Fundamentals of debt classification* (our debt classification white paper).

A debt classification issue that may arise for a debtor involves a revolving credit agreement (i.e., a revolver) with a fluctuating borrowing base, which is the maximum amount that can be borrowed under the revolver by the debtor and may depend on the carrying amount of one or more of the debtor’s balance sheet accounts, such as accounts receivable or inventory. The calculation of the borrowing base and how often it is reset depends on the terms of the revolver. When a revolver has a fluctuating borrowing base, the classification of its outstanding balance at the current balance-sheet date depends, at least in part, on whether outstanding balance exceeds: (a) the borrowing base as of the balance-sheet date or (b) the expected borrowing base(s) at any reset date(s) within one year of the current balance-sheet date.

Debtors should carefully consider the effects of the coronavirus pandemic on the calculation of their borrowing base as of the balance-sheet date, as well as those reset dates within one year of the balance-sheet date. Failure to consider any reductions in its borrowing base(s) due to the effects of the coronavirus pandemic on its operations and cash flows could result in the debtor classifying part of the revolver’s outstanding balance as noncurrent, when it should be classified as current. Additional information about the classification of revolvers with and without borrowing bases can be found in Section B.5 and Examples C.6 to C.11 of our debt classification white paper, with Examples C.7 and C.8 specifically illustrating the classification considerations for revolvers with borrowing bases.

**Modifications: Debtor accounting**

To the extent changes are made to its existing debt arrangements, a debtor must first determine whether those changes represent a TDR subject to the accounting requirements of ASC 470-60, “Debt – Troubled Debt Restructurings by Debtors,” and if not, whether those changes represent a modification or extinguishment subject to the accounting requirements of ASC 470-50, “Debt – Modifications and Extinguishments.” Additional information about determining the appropriate accounting model to apply when changes are made to debt, and about applying the appropriate accounting model to those changes, can be found in our white paper, *Fundamentals of accounting for debt modifications and restructurings*.

**Modifications: Lender accounting**

Lenders that are making modifications as a result of the coronavirus or otherwise will need to give consideration to ASC 310-40, “Receivables – Troubled Debt Restructurings by Creditors,” in determining whether the modification is a TDR. Our article, *Temporary relief for financial institutions: TDR accounting*, explains the relief that was provided to financial institutions by the Coronavirus Aid, Relief, and Economic Security (CARES) Act. Additionally, *Coronavirus: Interagency statement on loan modifications* provides financial reporting information relevant to TDRs, and while this information is also geared to supervised financial institutions, on March 22, 2020, the FASB issued a release indicating its agreement with this interpretation of the accounting literature on TDRs. Accordingly, entities not subject to supervision also
may find the interagency statement helpful when applying ASC 310-40. ASC 310-20-35 is the relevant guidance to consider by creditors for modifications that are not deemed to be a TDR.

Lenders may provide a loan payment holiday to borrowers affected by the coronavirus pandemic, which allows the borrowers to temporarily cease making payments without interest accruing during the holiday. When the application of U.S. generally accepted accounting principles (GAAP) to the specific facts and circumstances of the loan payment holiday do not result in a TDR or a new lending arrangement, but instead results in the application of the modification accounting model in ASC 310-20, “Receivables – Nonrefundable Fees and Other Costs,” the FASB staff has indicated that either of the following two accounting models are acceptable with respect to accounting for interest income during the holiday:

- Interest income is recognized during the loan payment holiday using a revised effective interest rate that equates the modified debt’s remaining cash flows to the current carrying amount of the debt. The revised effective interest rate is used prospectively over the remaining term of the debt.

- Interest income is not recognized during the loan payment holiday. Instead, interest income should be recognized based on the modified contractual terms of the loan. Recognition of interest income resumes at the end of the loan payment holiday.

We believe the model elected by a lender should be consistently applied and disclosed as its accounting policy.

The American Institute of Certified Public Accountants (AICPA) issued Q&A Section 2130.41, Loan Restructurings Resulting in Periods with Reduced Payments—Determination of the Effective Interest Rate, which addresses how to determine the effective interest rate for restructured loans that are neither required to be accounted for as TDRs nor new loans.

**Business interruption insurance considerations**

Careful consideration should be given to insurance policies to understand which losses are covered and which are excluded. ASC 450-30, “Contingencies – Gain Contingencies,” addresses the recognition and disclosure of gain contingencies which, by definition, involve uncertainty as to the possible gain that will ultimately be resolved. Under its provisions, contingencies that might result in a gain should not be recognized. The ultimate recovery under a business interruption policy is highly judgmental and typically subject to substantial negotiations between the insured and the insurance company. Consequentially, business interruption insurance recoveries are generally not recognized until the proceeds are received or the insurer confirms the amount of proceeds to which the insured is entitled, such that the uncertainty is removed.

**Obligations for exit or disposal costs and contingencies**

Forced business closures and distressed economic conditions are likely to lead to workforce reductions and (or) consolidation, disposal or abandonment of certain facilities. Additionally, these factors, as well as others that include travel bans and prohibitions on large group gatherings, will likely lead to contract terminations. ASC 420, “Exit or Disposal Cost Obligations,” addresses liability recognition for certain termination benefits, contract termination costs and other exit and disposal costs. ASC 450, “Contingencies,” addresses recognition and disclosure of both gain and loss contingencies.

**Revenue recognition**

**Variable consideration**

Variable consideration can take many forms, including refunds, returns, discounts, rebates, performance bonuses, milestone payments, penalties, contract claims and price concessions. An estimate of the variable consideration to which an entity expects to be entitled should be included in the transaction price (and ultimately recognized as revenue) to the extent it is probable that its inclusion will not result in a significant reversal of cumulative revenue recognized when the uncertainty giving rise to the variability is
resolved. The estimate of variable consideration must be reassessed each reporting period until the underlying uncertainty is resolved. An entity’s previous estimates of variable consideration may significantly change in the current environment. For example, there may be more product returns and resulting refunds than originally anticipated, the criteria for earning certain performance bonuses may no longer be likely to be met, or there may be unanticipated penalties incurred that would warrant a reduction to previously recognized revenue and may impact future revenue recognition.

**Contract modifications**

Contract modifications occur when the entity and its customer agree to add or change enforceable rights and obligations in the contract (e.g., changes to the contract’s scope and [or] price). The accounting model applied to a contract modification under ASC 606, “Revenue from Contracts with Customers,” depends on a number of factors, including the pricing of the modification, whether any new products or services added by the modification are distinct and whether any of the remaining goods or services are part of a partially satisfied single performance obligation. Depending on the facts and circumstances, a contract modification could be accounted for under ASC 606-10-25-12 and 25-13 as: (a) a separate contract, (b) the termination of one contract and execution of a new contract (which results in prospective treatment) or (c) part of the original contract (which could result in the recognition of a cumulative catch-up adjustment). In the current environment, there may be significant contract modifications occurring involving changes in scope, price changes or a combination of both. When considering contracts in which price concessions are granted, entities will first need to evaluate whether that price concession is considered a change to variable consideration (in which case it would result in a change in the estimated transaction price) or a contract modification (in which case the contract modification guidance included in ASC 606-10-25-12 and 25-13 would apply).

**Collectibility**

An entity must conclude that collection of substantially all of the amount to which it will be entitled in exchange for the goods or services that will be transferred to the customer is probable (i.e., likely to occur) in order to conclude a contract with a customer exists under ASC 606. An evaluation of collectibility is also required for existing contracts that previously were determined to meet the collectibility criterion if there is a significant change in facts and circumstances. An example of a significant change in circumstances related to whether collectibility continues to be probable is a significant deterioration in a customer’s credit risk and ability to access credit due to the loss of major customers. If this criterion is not met at contract inception or upon re-evaluation due to a significant change in facts and circumstances, the entity should reassess the criteria in subsequent reporting periods (as necessary) to determine whether all of the criteria subsequently are met. Until this criterion (among others) is met, an entity must defer revenue (or stop recognizing future revenue in the case of a re-evaluation) until the three criteria noted at ASC 606-10-25-7 are met. Additionally, any existing accounts receivable related to contracts that were re-evaluated and determined to no longer meet the collectibility criterion generally would be accounted for under ASC 310, “Receivables,” or ASC 326-20 upon its adoption, with any impairment loss presented as an expense and not a reduction of revenue. While under typical circumstances an entity would meet this criterion when entering into a revenue contract and would not be required to re-evaluate this criterion for ongoing contracts, in the current environment heightened scrutiny should be placed on this evaluation.

**Revenue recognition over time**

If an entity satisfies performance obligations over time, it must recognize revenue over time using the method that best measures the progress made in transferring control of the underlying goods or services to the customer. Output methods or input methods can be used to measure progress toward complete satisfaction of performance obligations, which is calculated at the end of each reporting period. The calculation is based on the amount of outputs or inputs to date and the estimated total amount of outputs or inputs necessary to satisfy the performance obligation. When using an input method to measure
progress, such as a cost-to-cost method, any cost incurred that ultimately does not contribute to satisfying the performance obligation should be removed from both the numerator and denominator of the cost-to-cost measure in determining the revenue recognized. Costs that ultimately do not contribute to satisfying the performance obligation may be caused by significant unexpected inefficiencies in the entity’s performance (e.g., wasted labor, material, other resources) that were not included in the entity’s contract price. In the current environment, these types of inefficiencies may be more prevalent, and entities should consider this closely when evaluating the amount of revenue recognized over time.

Hedge accounting and derivative valuation

Factors such as reduced sales and supply chain and other disruptions associated with the coronavirus pandemic also could impact the continued application of hedge accounting. When hedging forecasted transactions, such as interest payments on variable-rate debt, sales or purchases of a specific commodity or sales or purchases that are denominated in a certain currency, ASC 815-30-40 requires hedge accounting to be discontinued if any criteria to apply hedge accounting are no longer met, including the criterion in ASC 815-20-25-15(b) that requires hedged forecasted transactions to be probable of occurring. Additionally, when the determination is made that it is probable that a hedged transaction will not occur within the originally documented time period (or the two-month period thereafter), generally amounts reported in accumulated other comprehensive income (AOCI) related to the hedging derivative must be immediately reclassified to earnings. ASC 815-30-40-4 provides an exception to the immediate reclassification for rare cases—when the existence of extenuating circumstances that are related to the nature of the forecasted transaction and that are outside the control or influence of the reporting entity cause the forecasted transaction to be probable of occurring on a date that is beyond the additional two-month period of time, immediate reclassification is not required. The FASB staff has indicated that delays attributable to the coronavirus pandemic qualify as one of those rare cases in which the timing exception applies. However, it must be emphasized that the timing exception only applies if the forecasted transaction remains probable of occurring over a time period that is reasonable considering the nature of the entity’s business, nature of the forecasted transaction and magnitude of the disruption to the entity’s business from the coronavirus pandemic. If at any time it is no longer probable that the forecasted transaction will occur within that reasonable time period, the timing exception would not apply, and the amounts deferred in AOCI related to the discontinued cash flow hedge would be immediately reclassified into earnings and disclosed in the financial statements. Careful consideration should be given to the specific facts and circumstances in determining whether a delayed forecasted transaction qualifies for this timing exception.

In addition, ASC 815-30-40-5 indicates that a pattern of determining that forecasted transactions are probable of not occurring calls into question an entity’s ability to accurately predict forecasted transactions and the ability to use cash flow hedge accounting in the future for similar transactions. The FASB staff believes, because of the unprecedented nature of the coronavirus pandemic, it would be acceptable for management to conclude that missed forecasts related to the coronavirus pandemic need not be considered when determining whether the entity has exhibited a pattern of missing forecasts that would call into question its ability to accurately predict forecasted transactions, and thus, the ability to use cash flow hedge accounting in the future for similar transactions. Determining whether the missed forecast is related to the coronavirus pandemic requires judgment based on the applicable facts and circumstances. If an entity determines that a missed forecast is related to the coronavirus pandemic, it continues to account for those missed forecasts in accordance with ASC 815-30-40-5 and to disclose the associated amounts as required by ASC 815-10-50.

In a letter dated May 1, 2020, the International Swaps and Derivatives Association (ISDA) requested relief, similar to that discussed in the preceding paragraphs, from the Securities and Exchange Commission (SEC) staff related to ongoing cash flow hedges in which the hedged forecasted transactions are interest payments that are expected to be delayed beyond the period specified in the hedge documentation due to the coronavirus pandemic. It is our understanding that the SEC staff indicated that
it would not object to an entity continuing cash flow hedge accounting in this circumstance if, amongst other requirements, the hedge relationship remains highly effective and the hedged forecasted interest payments remain probable of occurring. Reporting entities are encouraged to refer to the ISDA’s website for the details of this relief as we expect those details to be documented there at a later date.

In addition to giving consideration to whether hedged forecasted transactions remain probable, entities also should be mindful of other potential impacts the extreme market and economic conditions could have on the effectiveness of accounting hedges, particularly where there are some differences in critical terms. Examples may include that the derivative and hedged item may have been linked to different commodities indices that were highly correlated in the past but are not highly correlated now. Another common example is variable-rate debt with a floor that is hedged through an interest rate swap that does not have a floor. The current low interest rate environment may exacerbate that difference in critical terms. Entities may find when performing their quantitative assessments of effectiveness under the time frames prescribed by ASC 815-20, “Derivatives and Hedging – Hedging—General,” (generally, at a minimum quarterly) that certain hedges are no longer highly effective, in which case, hedge accounting should be discontinued. Additionally, entities that are assessing effectiveness qualitatively under ASC 815-20-35-2A may find that the conditions are such that the entity no longer can assert qualitatively that the hedging relationship was and continues to be highly effective. In that case, the quantitative method selected in the initial hedge documentation would need to be performed to determine if the hedge relationship remains highly effective.

As it relates to derivative valuation, entities are reminded of the need to incorporate the risk of nonperformance into derivative valuations to arrive at a fair value measurement that is consistent with ASC 820. This requirement applies to derivatives that are designated as hedging instruments and those that are not. While this requirement is not new, as a consequence of current economic conditions and the duress certain entities are under, nonperformance risk can have a more significant impact on the valuation of a derivative, particularly for those contracts that are not fully collateralized on a daily basis by whichever party is in a liability position on that day. With forward contracts, such as interest rate swaps that potentially involve a two-way transfer of cash, the measurement should consider the risk of nonperformance of both parties to the contract.

**Stock compensation**

Share-based payment arrangements may include performance targets tied to an entity’s operations (e.g., customer sales, revenues, annual earnings before interest, taxes, depreciation and amortization). Under ASC 718, “Compensation—Stock Compensation,” entities are required to assess the outcome of the performance condition and update that assessment each reporting period. Compensation cost is recorded only if it is probable the performance condition will be achieved. Probable, as used in this assessment, means an event is likely to occur. Disruptions in operations caused by the response to the coronavirus pandemic may result in a change to this probability assessment. Entities will need to carefully assess whether performance conditions are still probable of being achieved and adjust compensation cost accordingly.

As a consequence of the declines in operations or a downturn in the market, entities may also be considering changing the terms of share-based payment arrangements to allow for continued vesting in awards with performance conditions or to lower the exercise price for out-of-the-money options. Any amendments that impact the vesting, value or classification of share-based payment awards must be accounted for as modifications and could result in changes in the amount of compensation cost to be recognized.

**Tax considerations**

On March 27, 2020, the President signed the CARES Act into law. The Act includes several significant provisions for corporations, including increasing the amount of deductible interest under section 163(j), allowing entities to carryback certain net operating losses (NOL), and increasing the amount of NOL that
corporations can use to offset income. These changes may have significant effects on an entity’s provision for income taxes, especially where entities have NOL or section 163(j) carryforwards and a valuation allowance against some or all of their deferred tax assets. RSM’s Tax Alert provides more information regarding the changes and the accounting for the tax provisions of the CARES Act.

Under ASC 740-10-45-15, entities should include the effects of any tax law changes in the financial statement period including March 27, 2020, the date of enactment. Accordingly, the tax law changes should not be reflected in the income tax provision for periods ending prior to the date of enactment. Instead, entities that are still in the process of preparing financial statements for such periods should quantify the expected impact of the CARES Act and consider whether the effects are significant enough to warrant a disclosure describing the expected effect of the Act on their financial statements.

Additionally, consideration should be given to the interim reporting requirements in ASC 740-270, “Income Taxes – Interim Reporting,” (as relevant) to determine the estimated annual effective tax rate to apply.

**Consolidation**

ASC 810-10-35-4 provides examples of events that, if one occurs, requires reconsideration of whether a legal entity is a variable interest entity (VIE). In the current economic environment, an entity might incur significant losses, which might exceed expected losses as calculated under ASC 810, “Consolidation.” Incurring such operating losses generally does not trigger the requirement to reassess whether the entity is a VIE. However, it is possible that, in response to significant losses, an entity might take an action that constitutes a reconsideration event. For example, if a VIE refinances its debt or receives additional equity contributions from new or existing equity holders, that would require reconsideration of whether the entity is a VIE.

Additionally, ASC 810 requires reporting entities to continually reassess whether they are the primary beneficiary of a VIE. It is also possible that changes in circumstances arising from the coronavirus pandemic might result in changes to previous conclusions as to whether the reporting entity is the primary beneficiary of the VIE. For example, assume the entity in the example in the previous paragraph was considered a VIE prior to defaulting on its debt, and that the reporting entity is the primary beneficiary. As a consequence of the lender obtaining the ability to make the decisions that most significantly impact the economic performance of the VIE, the reporting entity likely no longer will be the primary beneficiary.

**Paycheck Protection Program loans and other government assistance**

**Paycheck Protection Program loans**

The CARES Act established the Paycheck Protection Program (PPP), which is administered by the U.S. Small Business Administration (SBA), to provide loans to qualifying entities. Under this program, a qualifying entity may apply to an SBA-approved lender for a federally guaranteed loan to help offset certain payroll and other operating costs (e.g., rent and utility costs). The loan and accrued interest, or a portion thereof, is eligible for forgiveness by the SBA if the qualifying entity meets certain conditions. The SBA has published Paycheck Protection Program Loans Frequently Asked Questions (FAQs) for Lenders and Borrowers (PPP FAQ for lenders and borrowers), which provides guidance on a variety of issues, including an indication in Questions 39 and 46 that entities with loans in excess of $2 million will be subject to audit to determine whether they truly qualified for the loan. The scrutiny of an audit for those loans in excess of $2 million may create an incremental degree of uncertainty with respect to whether the loans will have to be repaid. The SBA has also published Paycheck Protection Program Frequently Asked Questions (FAQs) on PPP Loan Forgiveness (PPP FAQ on loan forgiveness), which provides guidance on a whole range of issues having to do with the forgiveness of PPP loans, such as completing the loan

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1 See Questions 31 and 37 of the SBA’s PPP FAQ for lenders and borrowers for liquidity considerations related to whether an entity qualifies for the loan.
forgiveness application, determining whether payroll and nonpayroll costs are eligible for loan forgiveness and assessing how the forgiveness amount may be affected by workforce reductions. Whether an entity qualifies for a PPP loan, and whether it meets the necessary conditions for forgiveness, requires careful consideration of the PPP requirements and the individual entity’s facts and circumstances.

**Borrower accounting**

There is currently no specific guidance in U.S. GAAP that addresses the accounting when a business entity obtains a loan that is forgivable by a government entity. Based on the discussion in the remainder of this section, we believe the following accounting models should be considered by business entities and not-for-profit entities (as appropriate):

<table>
<thead>
<tr>
<th>Fact pattern</th>
<th>Business entities</th>
<th>Not-for-profit entities</th>
</tr>
</thead>
<tbody>
<tr>
<td>When the entity determines it did not qualify for the loan</td>
<td>ASC 470, “Debt”</td>
<td>ASC 470</td>
</tr>
<tr>
<td>When the entity does not expect to meet the conditions for some or all of the forgiveness of the loan</td>
<td>ASC 470 for the portion of the loan for which the entity does not expect to meet the forgiveness conditions (see next row for the portion for which the entity expects to meet the forgiveness conditions)</td>
<td>ASC 470 for the portion of the loan for which the entity does not expect to meet the forgiveness conditions (see next row for the portion for which the entity expects to meet the forgiveness conditions)</td>
</tr>
</tbody>
</table>
| When the entity determines that it does qualify for the loan and expects to meet the conditions for forgiveness of the loan | ASC 470 or one of the following by analogy\(^2,3\):  
  - International Accounting Standards (IAS) 20, *Accounting for Government Grants and Disclosure of Government Assistance*  
  - ASC 958-605, “Not-for-Profit Entities – Revenue”  
  - ASC 450-30 | ASC 470 or ASC 958-605 |

We believe that accounting for a PPP loan as debt is acceptable for both business and not-for-profit entities, and certainly warranted when they expect to repay the loan or do not expect the loan to be forgiven. In addition, when an entity is considering whether a model other than ASC 470 may be appropriate, it should carefully consider whether it qualifies for the loan and meets the necessary conditions for forgiveness of the loan by the SBA. This would include consideration of the SBA announced audit of loans over $2 million. At this time, the timing and objective-versus-subjective nature of the audit are unknown, which may make it difficult for entities to determine if, upon audit, the entity will be required to repay the loan.

Because there is currently no specific guidance in U.S. GAAP that addresses the accounting when a business entity obtains a loan that is forgivable by a government entity, the SEC staff in the Office of the Chief Accountant were asked to specifically comment on whether they would accept a registrant’s use of

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\(^2\) In determining the appropriate guidance to apply, a business entity should consider its previous accounting policy for similar transactions (if any).

\(^3\) The SEC staff’s views are provided later in this section.
either of the following models to account for a PPP loan: (a) ASC 470 or (b) IAS 20 by analogy. Additional
discussion of both of these approaches is provided later in this section. We understand that when
considering these two models, the SEC staff made it clear that by providing their views, they were not
commenting on whether a registrant is or is not eligible to receive a PPP loan. The SEC staff indicated
they would not object to a registrant accounting for the loan as debt under ASC 470, nor would they
object to a registrant concluding that a PPP loan is akin to a government grant and accounting for it by
analogy to IAS 20, provided the registrant qualifies for the loan and there is reasonable assurance that it
will meet the conditions necessary for forgiveness of the loan by the SBA. For this purpose, the concept
of reasonable assurance equates to probable as used in ASC 450. The SEC staff did not comment on
other guidance that may or may not be appropriate for a registrant to apply when accounting for PPP
loans.

The AICPA issued Q&A Section 3200.18, Borrower Accounting for a Forgivable Loan Received Under the
Small Business Administration Paycheck Protection Program, to address accounting for PPP loans by
borrowers that are nongovernmental entities. The guidance in the AICPA Q&A related to the accounting
model(s) that should or may be applied in certain facts and circumstances is consistent with the
discussion herein.

While there is no specific guidance in U.S. GAAP with respect to how business entities should account for
forgivable loans, there is specific guidance for how not-for-profit entities should account for contributions
(which include the forgiveness of liabilities) in ASC 958-605. Despite ASC 958-605 specifically excluding
from its scope transfers of assets from government entities to business entities, at a meeting of the
Private Company Council on April 17, 2020, the FASB staff noted that business entities are not precluded
from applying ASC 958-605 by analogy when appropriate. As such, this guidance could potentially be
applied by a business entity by analogy if the entity believes the liability will be forgiven. If that is not the
case, the entity would account for the loan as debt under ASC 470. Additional information about ASC
958-605 is provided later in this section.

In addition to accounting for a PPP loan in accordance with ASC 470 or by analogy to IAS 20 or ASC
958-605, we believe it may also be acceptable for business entities to account for the forgiveness of the
loan in accordance with the guidance in ASC 450-30, for which additional information is provided next.

Following is additional information about each of the accounting models discussed herein (refer to the
preceding table for a summary of our thoughts on which entities may apply each model and under which
circumstances):

- **ASC 470.** The amounts received under the loan are recognized as debt. Interest expense should be
  accrued and recognized on the loan in accordance with ASC 835-30, “Interest – Imputation of
  Interest.” However, an entity should not impute interest based on a higher market rate (as otherwise
  required), because an exception to doing so is provided in ASC 835-30-15-3(e) when the interest rate
  is prescribed by a government agency. For derecognition purposes, ASC 470-50-40-1 refers to ASC
  405-20-40-1, which indicates that a financial liability is not derecognized until it is either paid off by the
debtor or the debtor is legally released as the primary obligor. For this purpose, a financial liability
includes debt and any accrued interest. Any gain that should be recognized upon being legally
released (because the loan and any accrued interest is forgiven in whole or in part) is presented in
the income statement as a gain on the extinguishment of debt. For purposes of the cash flow
statement, when the loan proceeds are received, they should be classified as a financing cash inflow.
In addition, any portion of the loan forgiven should be disclosed as a noncash financing activity. any
portion of the loan repaid should be classified as a financing cash outflow and any interest paid
should be classified as an operating cash outflow.

- **IAS 20.** The loan is accounted for as a government grant by analogy to IAS 20, provided the business
  entity qualifies for the loan and there is reasonable assurance that it will meet the conditions
  necessary for forgiveness of the loan by the SBA. Under IAS 20, the forgivable loan would be
considered an income grant. As an income grant, the amounts received under the loan should be reflected as a deferred income liability on the balance sheet and derecognized into income as the entity is incurring and recognizing the qualifying payroll and other operating costs. The income statement effects of an income grant are presented as either a separate line item, within other income (or a similar general line item) or net within the related expense line item (e.g. payroll expense). For purposes of the cash flow statement, a business entity should classify the loan proceeds that are probable of forgiveness as either a financing or operating cash inflow, depending on its interpretation of the guidance in ASC 230, “Statement of Cash Flows.”

- **ASC 958-605.** Proceeds from the PPP loan should be accounted for as a conditional contribution and recognized as a refundable advance until the conditions for forgiveness have been substantially met or explicitly waived. The derecognition of the liability is reflected as contribution revenue (or other income, if appropriate) for a not-for-profit entity. When analogizing to ASC 958-605, we believe the derecognition of the liability for a business entity should generally be reflected in other income.

- **ASC 450-30.** Proceeds from the PPP loan should be recognized as a liability. A contingent gain is usually not recognized until all uncertainty is removed (i.e., all conditions for forgiveness are met).

Given the lack of guidance that is directly on point, as well as the subjectivity and complexities in determining if an entity is eligible for a loan and if the relevant criteria are met to release the liability into the income statement, we recommend an entity discuss the model selected and its application of that model with its advisers and auditors.

Any entity that obtains a PPP loan should provide clear and complete disclosure about the loan, including its terms, how the entity determined it was qualified to receive the loan, and how the entity is accounting for the loan and presenting it in its financial statements. In addition, SEC registrants should consider the effects of obtaining a PPP loan on other aspects of its filings with the SEC, including its risk factor and liquidity disclosures. For example, the SEC staff in the Office of the Chief Accountant indicated that if an SEC registrant would not have had the necessary cash flows to continue its operations without the PPP loan, it should disclose that fact. In addition, on June 23, 2020, the SEC staff in the Division of Corporation Finance issued Disclosure Guidance: Topic No. 9A, Coronavirus (COVID-19) – Disclosure Considerations Regarding Operations, Liquidity, and Capital Resources (CF Disclosure Guidance Topic No. 9A), to provide the staff's current views regarding disclosures about operations, liquidity and capital resources that SEC registrants should consider with respect to the business and market disruptions related to COVID-19, including disclosure considerations related to governmental financial assistance in the form of loans.

Because the administration of the PPP by the SBA is fluid, and its terms potentially subject to change as a result of future legislation, entities should monitor developments by referring to the Paycheck Protection Program page of the SBA’s website and the SBA’s PPP FAQ for lenders and borrowers and PPP FAQ on loan forgiveness. In addition, more guidance may be forthcoming with respect to the accounting for PPP loans. If such guidance is made available, this white paper will be updated to reflect it. Check back here for updates.

**Lender accounting**

Lenders of PPP loans have clear accounting guidance to follow. Namely, ASC 310-10, “Receivables – Overall,” addresses the general accounting for loans and other receivables and ASC 310-20 addresses the recognition and measurement of origination fees and costs.

Under ASC 310-10, a lender would account for the PPP loan as either held-for-sale or held-for-investment, based on its intention. Alternatively, a lender could elect the fair value option (FVO) to account for its PPP loans in accordance with ASC 825, “Financial Instruments.” The following is a summary of the initial and subsequent measurement for the possible classifications of PPP loans:
<table>
<thead>
<tr>
<th>Classification</th>
<th>Initial measurement</th>
<th>Subsequent measurement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loans held-for-investment</td>
<td>Amount lent plus deferred direct loan origination costs less the deferred origination fees received.</td>
<td>Amortized cost. The direct loan origination costs and fees are recognized over the term of the loan as a yield adjustment (interest income). If certain conditions are met, estimated prepayments can be used to shorten the term of the loan for the purpose of recognizing deferred costs and fees (see discussion later in this section).</td>
</tr>
<tr>
<td>Loans held-for-sale</td>
<td>Amount lent plus deferred direct loan origination costs less the deferred origination fees received.</td>
<td>Lower of amortized cost or fair value. The direct loan origination costs and fees are a component of the loan’s amortized cost basis and are not amortized, but rather impact the gain or loss on sale.</td>
</tr>
<tr>
<td>FVO</td>
<td>Fair value</td>
<td>Fair value</td>
</tr>
</tbody>
</table>

PPP loans will be repaid by either the borrower or the SBA. A lender would generally not recognize an allowance for loan losses for properly underwritten PPP loans because the SBA guarantees 100% of the principal and interest amounts.

For loans that are not accounted for at fair value, direct loan origination costs and fees are deferred as part of the amortized cost basis of the loan. We believe that fees received from the SBA should be deferred in this manner. As discussed in ASC 310-20, direct loan origination costs and fees on loans classified as held-for-investment are generally recognized as a yield adjustment to interest income using the effective interest method over the term of the loan. However, due to their forgivable nature, a PPP loan may have an actual life that is shorter than its term. ASC 310-20-35-26 allows lenders to consider estimated prepayments when determining the amortization period for recognizing the loan origination costs and fees if the lender holds a large number of similar loans for which prepayments are probable and the timing and amount of prepayments can be reasonably estimated. We believe, in the case of PPP loans, the loan forgiveness could be considered a prepayment. This means that the lender can elect to recognize loan origination costs and fees over a time horizon that is shorter than the term of the loan if the conditions discussed in ASC 310-20-35-26 are met. Consideration should be given to ASC 450 to determine if a loss should be recognized for fees that may be subject to clawback (because, for example, the borrower was not eligible for the loan).

The AICPA issued the following guidance, which provides further information about the lender’s accounting for PPP loans:

- Q&A Section 2130.42, Classification of Advances Under the Paycheck Protection Program
- Q&A Section 2130.43, Consideration of the SBA Guarantee Under the Paycheck Protection Program
- Q&A Section 2130.44, Accounting for the Loan Origination Fee Received from the SBA
Other government assistance

A number of governments around the world have considered or even implemented measures that provide assistance to entities that are attempting to deal with the financial impact of the coronavirus pandemic. These programs may be in various forms, including but not limited to loans (see the previous section for one type of loan), grants or tax relief. One example of such assistance is the CARES Act, passed in the United States on March 27, 2020.

The accounting for such assistance is generally dependent in large part on the form of the assistance:

- Income tax credits are accounted for under ASC 740, “Income Taxes,” as discussed in the “Tax considerations” section of this whitepaper.
- Loans generally are accounted for as debt under ASC 470 (see the previous section for discussion related to the accounting for PPP loans).
- Contributions should be accounted for in accordance with ASC 958-605.
- Assistance that represents a payment for goods or services would be considered revenue and accounted for under ASC 606.
- Assistance that does not fall into any of the preceding categories generally is viewed as a government grant.

U.S. GAAP does not provide guidance on accounting by business entities for government grants. ASC 958-605 provides guidance for not-for-profit entities. As noted in the previous section, despite ASC 958-605 specifically excluding from its scope transfers of assets from government entities to business entities, it may be appropriate for business entities to apply ASC 958-605 by analogy. Although, while the income-statement effects of a grant for a not-for-profit entity may be reflected as contribution revenue (or other income, if appropriate), the income-statement effects of a grant for a for-profit entity analogizing to ASC 958-605 should generally be reflected in other income. In certain cases, it may also be appropriate for business entities to analogize to IAS 20, which differentiates grants related to assets from grants related to income. Asset grants generally contain a primary condition that an entity qualifying for the grant purchase, construct or otherwise acquire long-term assets. When recognition of an asset grant is appropriate under IAS 20, it is recognized as either: (a) a deferred income liability (which is recognized in income on a systematic basis over the related asset’s useful life) or (b) a reduction in the carrying amount of the related asset (which is recognized in income as the asset is depreciated). Income grants are grants other than those related to assets. When recognition of an income grant is appropriate under IAS 20, it is reflected in the income statement on a systematic basis that is consistent with the entity’s recognition of the costs that qualify under the grant. Those income-statement effects are presented as either a separate line item, within other income (or a similar general line item) or net within the related expense line item for which the grant is intended to compensate the entity. Additional information about the guidance in IAS 20 applicable to income grants is provided in the previous section.

Entities should carefully analyze the substance of any governmental assistance, as well as their compliance with conditions of the assistance. Because of the current lack of guidance in U.S. GAAP, entities should remain abreast of viewpoints that may be expressed by standard setters. In addition, where multiple accounting policies are deemed acceptable, we believe it is important for an entity to adopt a policy that is consistently applied to similar assistance programs, and to disclose its accounting policy.

In CF Disclosure Guidance Topic No. 9A, the SEC staff in the Division of Corporation Finance provided its current views regarding disclosures about the short- and long-term effects that governmental financial assistance will have on an SEC registrant’s financial condition, results of operations, liquidity and capital resources, as well as the effects of that assistance on critical accounting estimates and assumptions.
Going concern, risks and uncertainties

If conditions or events related to the coronavirus raise substantial doubt about an entity’s ability to continue as a going concern within one year after the date the financial statements are issued (or available to be issued), certain financial statement disclosures are required under ASC 205-40, “Presentation of Financial Statements – Going Concern.” Additionally, ASC 275, “Risks and Uncertainties,” requires disclosures about risks and uncertainties including certain changes in estimates and vulnerability to concentrations that may be particularly relevant given current conditions. In certain cases, the circumstances related to the impacts of coronavirus on the entity’s operations, financial situation, or risks and uncertainties may warrant an emphasis-of-matter paragraph in the auditor’s report.

In CF Disclosure Guidance Topic No. 9A, the SEC staff in the Division of Corporation Finance provided its current views regarding disclosures when there is substantial doubt about an SEC registrant’s ability to continue as a going concern, including when the substantial doubt is alleviated by management’s plans.

For additional information about management’s responsibilities related to the going concern assessment, refer to our white paper, Going concern: Management’s evaluation during coronavirus pandemic.

Certain SEC and regulatory reporting considerations

The SEC and various regulators have provided delayed due dates for certain financial reporting requirements.

The SEC has reminded entities to provide investors with insights regarding their assessment of, and plans for addressing, material risks to their business resulting from the coronavirus. In addition to financial statement disclosures, specific risks may need to be disclosed in an SEC filing as risk factors. Also, among other required disclosures in management’s discussion and analysis of financial condition and results of operations, a registrant should describe any known trends or uncertainties that have had, or that the registrant reasonably expects will have, a material favorable or unfavorable impact on revenues or income. An entity may need to update previous disclosures to the extent that information becomes materially inaccurate.

On March 25, 2020, the SEC staff in the Division of Corporation Finance issued Disclosure Guidance: Topic No. 9, Coronavirus (COVID-19), to provide the staff’s current views regarding disclosure and other securities law obligations entities should consider with respect to COVID-19 and related business and market disruptions. SEC registrants also should keep in mind the requirement to disclose material changes in internal controls; for example, when preexisting controls can no longer be performed and (or) when new controls are put in place in response to necessitated operational changes resulting from the coronavirus pandemic.

On June 23, 2020, the SEC staff in the Division of Corporation Finance issued CF Disclosure Guidance Topic No. 9A to provide the staff’s current views regarding disclosures about operations, liquidity and capital resources that SEC registrants should consider with respect to the business and market disruptions related to COVID-19. The SEC staff’s views include a broad range of questions for SEC registrants to consider when determining the nature of the information they should disclose about the effects of COVID-19 on its operations, liquidity and capital resources (including the impacts of any related governmental financial assistance), as well as its ability to continue as a going concern.

GASB activities and resources

The Governmental Accounting Standards Board (GASB) has taken the following actions with respect to alleviating the financial reporting issues encountered by state and local governments due to the coronavirus pandemic:

- Provided effective date deferrals. The GASB issued Statement No. 95, Postponement of the Effective Dates of Certain Authoritative Guidance, which postpones the effective dates of almost all GASB
Statements and Implementation Guides that first became effective or are scheduled to become effective for state and local governments for periods beginning after June 15, 2018 and later. Statement 95 postpones the effective dates of many GASB Statements and Implementation Guides by one year, but also postpones the effective dates of Statement No. 87, Leases, and Implementation Guide No. 2019-3, Leases, by 18 months.

- Released guidance about the accounting and financial reporting issues related to the CARES Act and coronavirus pandemic. The GASB issued Technical Bulletin 2020-1, Accounting and Financial Reporting Issues Related to the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) and Coronavirus Diseases. The Technical Bulletin includes guidance related to the accounting for and financial reporting of various matters related to the coronavirus pandemic, such as resources received from the Coronavirus Relief Fund and forgivable PPP loans.

In addition, on the GASB Response to COVID-19 page of its website, the GASB provides links to a number of stakeholder resources, including its GASB Emergency Toolbox, which helps stakeholders quickly identify the relevant guidance for a variety of accounting and (or) financial reporting issues that may be of particular relevance during the coronavirus pandemic.

**Ongoing developments**

The financial reporting considerations related to the coronavirus pandemic are continuing to evolve. This white paper will be updated periodically as developments warrant. For additional resources related to the coronavirus pandemic, visit our Coronavirus Resource Center.