

Technical Line

FTC – final rule

Accounting considerations for intangible assets affected by the FTC's final noncompete rule

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What you need to know

- ▶ The FTC's final rule on noncompete arrangements generally prohibits employers from enforcing the terms of existing noncompete arrangements they have with workers. The rule also prohibits employers from entering into certain new noncompete arrangements.
- ▶ Companies that have recognized on their balance sheet a finite-lived intangible asset related to noncompete arrangements affected by the rule will need to consider the impact on the subsequent accounting of that asset.
- ▶ Companies should (1) evaluate the remaining useful life of any finite-lived intangible assets related to noncompete arrangements in each reporting period and (2) review the finite-lived intangible assets for impairment in accordance with ASC 360-10 when events or changes in circumstances indicate that the carrying amount of the long-lived asset may not be recoverable.
- ▶ While the rule is effective on 4 September 2024, legal challenges could impact its implementation. Companies should monitor developments in this area.

Overview

The Federal Trade Commission (FTC) recently issued a **final rule** prohibiting employers from enforcing certain existing noncompete arrangements and other similar provisions or clauses. The rule also prohibits employers from entering into certain new noncompete arrangements. Companies that have recognized a finite-lived intangible asset on their balance sheet that is related to noncompete arrangements affected by the FTC's prohibition will need to consider the rule's impact on the subsequent accounting of the asset.

The rule, which is effective on 4 September 2024, prohibits all noncompete arrangements, except for those that exist in the following scenarios:

- ▶ When a senior executive¹ arrangement is entered into before the effective date
- ▶ When an arrangement is made in connection with the bona fide sale of a business entity²
- ▶ When a non-compete-related cause of action is accrued before the effective date
- ▶ When there is a “good faith” belief that the FTC rule does not apply³

The rule does not apply to industries that are not regulated by the FTC.⁴

Key considerations

Noncompete agreements are legal arrangements that limit a person’s or an entity’s ability to compete with another entity in a specific market for a period of time. Companies may have noncompete arrangements recognized on their balance sheets as intangible assets. For example, if a target in a business combination has preexisting noncompete arrangements in place at the acquisition date, these arrangements typically would meet the contractual-legal criterion for recognition as intangible assets in a business combination.

Because the contractual provisions underlying most noncompete arrangements limit their useful life, these intangible assets are typically identified as finite-lived when they are initially recognized and are amortized over their estimated useful life in subsequent reporting periods, in accordance with Accounting Standards Codification (ASC) 350, *Intangibles – Goodwill and Other*. Finite-lived intangible assets are also reviewed for impairment in accordance with the guidance on impairment or disposal of long-lived assets in ASC 360-10, *Property, Plant, and Equipment – Overall*.

Reassessing the estimated useful life

ASC 350 requires a company to evaluate the remaining useful life of a finite-lived intangible asset each reporting period by determining whether certain events and circumstances have occurred that warrant a revision to the asset’s remaining amortization period.⁵

ASC 350-30-35-3 outlines six factors to consider when determining whether the estimate of the useful life should be changed, including the entity’s expected use of the asset and whether any legal, regulatory or contractual provisions exist that may limit the useful life. No factor should be viewed as more presumptive than another when an entity performs this evaluation.

If the estimate of an intangible asset’s useful life is changed, ASC 350 requires that the remaining carrying amount be amortized prospectively over the asset’s revised remaining useful life.⁶ See our Financial reporting developments (FRD) publication, *Intangibles – Goodwill and other*, for additional information.

How we see it

We believe a company that determines it has recognized intangible assets related to noncompete arrangements that would no longer be enforceable or provide benefit upon the effective date of the rule, would be required to shorten the asset’s estimated useful life to end at some point before or on the effective date. This determination will depend on the facts and circumstances of the underlying arrangement.

Impairment testing under ASC 360

Long-lived assets to be held and used, including finite-lived intangible assets (collectively, long-lived assets), are reviewed for impairment when events or changes in circumstances indicate that the carrying amount of the long-lived asset (or asset group) may not be recoverable (i.e., when there are impairment indicators).

One example of an impairment indicator that ASC 360 requires entities to consider is whether there is “a significant adverse change in legal factors or in the business climate that could affect the value of a long-lived asset (asset group), including an adverse action or assessment by a regulator.”⁷ If impairment indicators are present, a recoverability test is performed on an undiscounted basis to determine whether an impairment loss should be recognized. To perform the recoverability test, long-lived assets (and liabilities, if applicable) are grouped (i.e., the asset group) at the lowest level for which there are identifiable cash flows that are largely independent of the cash flows of other assets.

A company that identifies an impairment indicator specific to an individual asset included in an asset group should consider the significance of that individual asset to the asset group as a whole before proceeding with the recoverability test. If the impairment indicator is clearly specific to the individual asset and the individual asset is inconsequential to the asset group as a whole, performing a recoverability test may not be necessary. However, the company should evaluate whether it needs to modify the estimated useful life of the individual asset affected by the impairment indicator. See our FRD publication, [Impairment or disposal of long-lived assets](#), for additional information.

How we see it

Typically, noncompete arrangements that are recognized as intangible assets are part of a larger asset group when testing for impairment under ASC 360. As a result, noncompete arrangements may not be impaired in accordance with ASC 360 even if a company determines that it has recognized noncompete intangible assets that, upon the effective date of the rule, would no longer be enforceable or provide benefit.

What's next?

The FTC rule is effective on 4 September 2024. However, several lawsuits challenging the rule have been filed, and the outcome of the litigation, including the scope and whether the lawsuits will be resolved before the rule's effective date, is uncertain. Companies should continue to monitor developments in this area.

Endnotes:

- ¹ The rule defines a senior executive as “a worker who: (1) was in a policy-making position; and (2) received from a person for the employment: (i) total annual compensation of at least \$151,164 in the preceding year; or (ii) total compensation of at least \$151,164 when annualized if the worker was employed during only part of the preceding year; or (iii) total compensation of at least \$151,164 when annualized in the preceding year prior to the worker’s departure if the worker departed from employment prior to the preceding year and the worker is subject to a non-compete clause.”
- ² The rule states that it does “not apply to a non-compete clause that is entered into by a person pursuant to a bona fide sale of a business entity, of the person’s ownership interest in a business entity, or of all or substantially all of a business entity’s operating assets.”
- ³ The rule states that “it is not an unfair method of competition to enforce or attempt to enforce a non-compete clause or to make representations about a non-compete clause where a person has a good-faith basis to believe that this part is inapplicable.”
- ⁴ The FTC Act states that the FTC is empowered to regulate all persons, partnerships, or corporations, except banks, savings and loan institutions, Federal credit unions, common carriers, air carriers and foreign air carriers, and persons, partnerships, or corporations insofar as they are subject to the Packers and Stockyards Act. The FTC also does not regulate any entity that is not “organized to carry on business for its own profit or that of its members.” This means the rule may not apply to certain nonprofit entities.
- ⁵ ASC 350-30-35-9 states that “an entity shall evaluate the remaining useful life of an intangible asset that is being amortized each reporting period to determine whether events and circumstances warrant a revision to the remaining period of amortization. If the estimate of an intangible asset’s remaining useful life is changed, the remaining carrying amount of the intangible asset shall be amortized prospectively over that revised remaining useful life.”
- ⁶ ASC 350-30-35-9.
- ⁷ ASC 360-10-35-21.

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