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To the Point

FASB — proposed guidance

FASB proposes guidance on accounting for government grants by business entities

The proposal is based on the guidance in IAS 20 that many business entities currently apply by analogy to account for government grants.

What you need to know

- The FASB proposed establishing guidance on the recognition, measurement and presentation of a government grant received by a business entity to reduce diversity in practice.
- Many business entities currently analogize to IAS 20 to account for government grants due to the lack of authoritative guidance in US GAAP.
- In developing the proposal, the Board leveraged the guidance in that IFRS Accounting Standard, modifying certain aspects of its scope, recognition threshold and other implementation guidance.
- Comments are due by 31 March 2025.

Overview

The Financial Accounting Standards Board (FASB or Board) **proposed** amendments to establish guidance on the recognition, measurement and presentation of a government grant received by a business entity. US GAAP does not currently provide such guidance, and many business entities currently account for government grants by analogizing to International Accounting Standard (IAS) 20, *Accounting for Government Grants and Disclosure of Government Assistance*.

The FASB noted that when business entities apply IAS 20 or other US GAAP (e.g., Accounting Standards Codification (ASC or Codification) 958-605, *Not-For-Profit Entities — Revenue Recognition*) by analogy, they may not apply all of it. This has led to questions about the acceptability of certain accounting approaches and resulted in diversity in practice.

In response, the FASB proposed incorporating elements of IAS 20 into US GAAP, modifying certain aspects of IAS 20's scope, recognition threshold and other implementation guidance. The proposal is intended to reduce diversity in practice and create greater consistency because business entities would no longer have to analogize to other accounting models.

How we see it

Because the FASB based its proposal on IAS 20, business entities that previously analogized to ASC 958-605 or other guidance would likely be impacted the most by the proposed amendments.

Key considerations

Scope

The proposal would apply to all business entities (i.e., it would not apply to not-for-profit entities[1] and employee benefit plans in the scope of ASC 960, ASC 962 or ASC 965).

A government grant would be defined as "a transfer of a monetary asset or a tangible nonmonetary asset, other than an exchange transaction, from a government to a business entity." The guidance would not apply to exchange transactions (such as transactions in the scope of ASC 606, *Revenue from Contracts with Customers*), transactions in the scope of ASC 740 on income taxes, the benefit of below-market interest loans and government guarantees.

An entity would recognize a government grant when it is probable that the entity will comply with the grant's conditions and the grant will be received.

The Board provided examples of government grants that would be in the scope of the proposal, including transfers of cash or tangible nonmonetary assets (e.g., buildings, land, equipment), forgivable loans for which certain criteria for forgiveness are met and refundable tax credits not in the scope of ASC 740. The proposal would not apply to intangible assets or services, a reduction of an entity's liabilities (e.g., a sales, property or other tax abatement), government participation in the ownership of an entity and contributions to business entities from nongovernmental sources in the scope of ASC 958-605.

How we see it

Different terms can be used to describe various types of government assistance, such as grants, awards, subsidies and credits. Therefore, an entity should consider the facts and circumstances to determine whether assistance received from a government would meet the proposal's definition of a government grant.

Recognition, measurement and presentation

The proposal would require a business entity to recognize a government grant when it is probable that both (1) the entity will comply with the conditions attached to the government grant and (2) the government grant will be received. The proposal would replace the term "reasonable assurance" used in IAS 20 with "probable." The Board said[2] that reasonable assurance is generally interpreted to be consistent with the term probable as defined in the Master Glossary of the Codification.

Similar to IAS 20, the proposal would categorize government grants as either (1) grants related to assets (i.e., government grants whose primary condition is that an entity purchase, construct or otherwise acquire a long-term asset) or (2) grants related to income (i.e., those other than grants related to assets).

Grant related to an asset

Under the proposal, an entity would be able to elect one of the following approaches to account for a grant related to an asset:

- Under the deferred income approach, the entity would separately recognize (and present) the grant as deferred income on the balance sheet and recognize the government grant in earnings on a systematic and rational basis over the periods in which the entity recognizes as expenses the related costs for which the government grant is intended to compensate (e.g., the useful life of the asset). The entity would present the grant as part of earnings either separately under a general heading, such as other income, or by reducing the related expense (e.g., depreciation, gain or loss on sale, impairment).
- Under the cost accumulation approach, the entity would reflect the grant in the carrying amount of the asset on the balance sheet. There would be no separate subsequent recognition of the government grant proceeds in earnings because they have been reflected in the carrying amount of the asset used to determine depreciation or other subsequent accounting for that asset.

A government grant of a tangible nonmonetary asset (e.g., land) is a grant related to an asset. Under the proposal, an entity electing the deferred income approach would initially measure the tangible nonmonetary asset at fair value. An entity electing the cost accumulation approach would recognize the asset at the cost to the entity. IAS 20 provides for accounting for such grants at fair value but gives the option to measure nonmonetary assets at a nominal amount. However, this alternative under IAS 20 is not related to the presentation approach selected by the entity.

Grant related to income

A grant related to income would be recognized in earnings on a systematic and rational basis over the periods in which the entity recognizes as expenses the related costs for which the grant is intended to compensate. The entity would present the grant as part of earnings either separately under a general heading, such as other income, or by reducing the related expense.

How we see it

Similar to IAS 20, the proposal would allow for optionality regarding where an entity presents a grant related to an asset or a grant related to income, which could better reflect the economics of the grant and the effect of the grant on an entity's business or operations. Entities should adopt a presentation approach and consistently apply it to similar fact patterns.

Statement of cash flows

The proposal does not prescribe classification for the cash inflows of a government grant. The Board noted[3] that applying the guidance in ASC 230, *Statement of Cash Flows*, would result in classifying cash flows from government grants on the basis of the nature of the grant (i.e., depending on whether the cash flows from a government grant result from operating, investing or financing activities).

Disclosures

The proposal would require an entity to comply with existing annual disclosure requirements in ASC 832, *Government Assistance*. These required disclosures include that of the line items on the balance sheet and income statement that are affected by the grant and the amounts applicable to each financial statement line item in the current reporting period. Such a disclosure for a grant related to an asset accounted for under the cost accumulation approach would only be required in the period in which the grant is recognized on the balance sheet.

The proposal also would require an entity to disclose the fair value of a tangible nonmonetary asset that is received as a government grant in the period in which the grant is recognized on the balance sheet, regardless of whether the entity applies the deferred income approach or the cost accumulation approach. That is, the entity would need to disclose the fair value of the tangible nonmonetary asset even if it does not recognize the fair value in the financial statements under the cost accumulation approach.

Accounting for a government grant in a business combination

If an entity has not fully complied with the conditions of a government grant related to income, an acquirer would recognize and measure deferred income based on the proposed government grant model. Accordingly, the proposal would create an exception to the general recognition and measurement principle of ASC 805, *Business Combinations*, for government grant-related liabilities.

An acquirer would recognize any liability to repay government grant proceeds (e.g., repayment obligation) following the guidance in ASC 450, *Contingencies*.

Effective date and transition

The Board will determine the effective date and whether early adoption would be permitted after it considers stakeholder feedback on the proposal.

Entities would have the option to apply the guidance either (1) prospectively to government grants that either are not complete as of the effective date or are entered into after the effective date or (2) retrospectively through a cumulative-effect adjustment to the opening balance of retained earnings at the beginning of the earliest period presented.

A government grant is considered complete when all of its proceeds have been recognized in accordance with current guidance before the effective date of this proposed guidance. For a grant related to an asset that was accounted for by reflecting the grant in determining the carrying amount of the asset (i.e., the cost accumulation approach), proceeds are considered recognized when the grant is reflected in the carrying amount of the asset on the balance sheet. For all other government grants, proceeds are considered recognized when they have been recognized on the income statement.[4]

Endnotes:

1 A not-for-profit entity that receives a government grant would apply ASC 958-605.
2 Paragraph BC26 of the proposal's Background Information and Basis for Conclusions.
3 Paragraph BC44.
4 Paragraph BC60.