WILLIAMS MARSTON

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Five Accounting Issues to Consider for Q1 2020

Executive Summary

- The COVID-19 pandemic has had a sudden and dramatic impact on the economy and created significant uncertainty for the future
- There are accounting issues resulting from the COVID-19 pandemic with which many management teams do not have recent experience
- Companies should evaluate whether a going concern analysis is warranted
- Companies should evaluate whether an impairment of goodwill or indefinite lived intangible assets exists

Overview

The first quarter of 2020 is shaping up to be very challenging from an accounting and financial reporting perspective for many companies. The growing impact of COVID-19 on the healthcare system, economy and capital markets is unprecedented in modern U.S. history. After a decade of steady growth and acquisitions, many companies have accumulated significant goodwill and intangible asset balances on their balance sheets. At the same time, many accountants do not have experience with impairments and other analyses which many will need to conduct in short order to meet their filing deadlines. Here is an overview of five accounting issues management teams should start considering before the end of the quarter.

Going concern

Under ASC 205-40, an entity's financial statements are presented under the assumption that the entity will continue to operate as a going concern. This means the entity has the financial resources to operate for at least twelve months from the issuance date of the financial statements. If there is any doubt about a company's ability to operate for twelve months, management must demonstrate to their auditors that they can do so with a detailed cash flow forecast. If there is significant doubt about a company's ability to continue operating for at least 12 months, the entity must disclose the risks and assumptions inherent in their assessment in the footnotes to their financial statements.

- Companies should consider whether an impairment of long-lived or intangible assets subject to amortization exists
- Any amendments to debt agreements should be evaluated for the accounting impact
- Enhanced disclosure requirements may be necessary

Goodwill and indefinite-lived intangible assets

Goodwill and indefinite-lived intangible assets are tested for impairment at least annually and more frequently if events or circumstances indicate that it is more likely than not that an impairment exists. ASC 350 provides events and factors that should be considered in evaluating whether an interim impairment test is required for both goodwill and indefinite-lived intangible assets. Companies will need to consider the impact on the fair value of their reporting units and indefinite-lived intangible assets to determine whether an interim impairment test is required. ASC 350-30-35-18B provides examples of events that could affect the significant inputs used to determine the fair value of an indefinite-lived intangible asset.

Long-lived assets and intangible assets subject to amortization

Long-lived assets and intangible assets subject to amortization should be tested for recoverability when events or circumstances indicate that the carrying amount may not be recoverable. Similar to ASC 350, ASC 360 provides a listing of indicators in making this determination. If indicators are present, the company must test the asset or asset group for recoverability. If the carrying amount of the long-lived asset or asset group exceeds the estimated undiscounted cash flows, then the carrying amount of the long-lived asset or asset group is not recoverable. If it is determined that the carrying amount is not recoverable, an impairment loss should be recognized in the amount that the carrying amount of the long-lived asset or asset group exceeds its fair value.

Debt restructuring

Any time a credit agreement is modified, the borrower should consider whether it is a Troubled Debt Restructuring ("TDR"). The accounting for a TDR under ASC 470-60 can be significantly different from other modifications accounted for under ASC 470-50. In order for a modification to be considered a TDR, the borrower must be experiencing financial difficulties and the lender must grant a concession. ASC 470-60 provides guidance on determining whether a company is experiencing financial difficulties and whether a concession was granted. If it is not considered a TDR, the company should evaluate whether the restructuring should be accounted for as a modification or extinguishment under ASC 470-50.

Enhanced disclosures

The COVID-19 pandemic is a "Black Swan Event" which is something that is very rare, unexpected and potentially has serious consequences. Companies should

consider the GAAP and SEC disclosure requirements which may necessitate new and enhanced disclosure in multiple areas of their financial statements and SEC filings. The impact could include changes in estimates of demand for a company's products and services, effects on their vendors, liquidity, and in some cases solvency. Management should carefully review their disclosure of risks and uncertainties as well as subsequent events to ensure they are sufficient to address this significant event. Outside the financial statements, enhanced disclosure may be necessary in the risk factors and MD&A to address the sudden and significant change in future expectations.

Management teams should also be aware of the requirement to file a Form 8-K within four business days after a decision is made to record a material charge for impairment to one its assets, including impairments of securities or goodwill. However, there is no requirement to disclose this on Form 8-K if the decision is made in connection with the preparation, review or audit of financial statements required to be included in the next periodic report, if the periodic report is filed on a timely basis and the conclusion is disclosed in the report. Accordingly, a filing may not be required if an impairment was identified as part of the preparation of the Q1 2020 interim financial statements and was disclosed in a Form 10-Q that was filed timely.

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