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Accounting Standards: FASB Updates Private Company Accounting Issues

Publicly traded companies in the U.S. are required to follow Generally Accepted Accounting Principles (U.S. GAAP). But many privately held companies, including many manufacturers and distributors, find U.S. GAAP to be too complicated and costly, and somewhat irrelevant to users of their financial statements.

In order to simplify financial statement reporting for private companies, the Financial Accounting Foundation formed the Private Company Council (PCC). The PCC works with the Financial Accounting Standards Board (FASB) to determine whether there should be differences in U.S. GAAP for public and private companies.

In the summer of 2013, the FASB issued for public comment three PCC-developed proposals involving accounting for intangible assets acquired in business combinations, goodwill, and certain types of interest rate swaps. Earlier this year, the FASB endorsed two of the proposals and issued updates to U.S. GAAP for private companies relative to two of the three issues. The board also issued a third update regarding certain leasing arrangements.

Accounting for Goodwill

Accounting Standards Update No. 2014-02 allows a private company to subsequently amortize goodwill on a straight-line basis over a period of 10 years, or over a shorter period if the company demonstrates that another useful life is more appropriate. It also permits a private company to use a simplified impairment model for goodwill.

According to the new standard, goodwill should be tested for impairment "when a triggering event occurs that indicates that the fair value of a company, or a reporting unit, may be below its carrying amount." If your company chooses this alternative, it must also make an accounting policy election to assess goodwill for impairment either at the company level or the reporting unit level.

If your company carries goodwill on its balance sheet, the amortization method and the less frequent goodwill impairment testing should result in significant cost savings.

Interest Rate Swaps

Under Accounting Standards Update No. 2014-03, non-financial institution private companies now have the option to use a "simplified hedge accounting approach to account for interest rate swaps that are entered into for the purpose of economically converting variable-rate interest payments to fixed-rate payments," according to the FASB.

When a private company uses this simplified accounting approach, "the income statement charge for interest expense will be similar to the amount that would result if the company had directly entered into a fixed-rate borrowing instead of a variable-rate borrowing and an interest rate swap."

The update also allows companies to recognize the swap using its settlement value — which measures the swap without non-performance risk — instead of at fair value.

Leasing Arrangements

Accounting Standards Update No. 2014-07 gives private companies an alternative to U.S. GAAP in applying variable interest entity (VIE) guidance to certain common control leasing arrangements. The standard allows a company to elect — when four specific conditions are met — not to apply VIE guidance to a lessor under common control. Instead, the company simply makes certain disclosures about the lessor and the leasing arrangement.

The FASB believes these disclosures provide useful lessor-related information for users of private company financial statements while reducing costs and complexity for private company lessees that apply VIE guidance.

We hope you find this information valuable. Contact us to discuss your NIIT planning opportunities and any other questions or needs you may have as year-end draws near.

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