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# FASB and PCC Eliminate Effective Dates and Clarify Transition Guidance for Private Company Alternatives

The FASB recently issued an Accounting Standards Update (ASU) that eliminates the effective dates for four private company accounting alternatives developed by the Private Company Council (PCC).[1] The ASU is effective immediately, and allows a private company to elect any of the PCC alternatives at the beginning of any annual reporting period for the first time without assessing preferability.[2]

## Key Facts

The new ASU applies to four FASB ASUs that provide PCC alternatives:

- 2014-02, *Accounting for Goodwill*;
- 2014-03, *Accounting for Certain Receive-Variable, Pay-Fixed Interest Rate Swaps – Simplified Hedge Accounting Approach*;
- 2014-07, *Applying Variable Interest Entities Guidance to Common Control Leasing Arrangements*; and
- 2014-18, *Accounting for Identifiable Intangible Assets in a Business Combination*.

The ASU allows a private company to apply specialized transition for the simplified hedge accounting and goodwill amortization alternatives regardless of when the company elects them.

## Key Impacts

- Eliminates the need to assess preferability, and provides specialized transition guidance to give private companies greater flexibility to decide whether and when to adopt a PCC alternative.
- This flexibility may further challenge financial statement users who compare private company financial results to the results of other companies.

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[1] Accounting Standards Update No. 2016-03, Effective Date and Transition Guidance, a consensus of the Private Company Council, available at www.fasb.org.

[2] FASB ASC Topic 250, Accounting Changes and Error Corrections, available at www.fasb.org.

## Background

The PCC added this issue to its agenda in response to stakeholders' concerns that some private companies may not elect PCC accounting alternatives at their effective dates because (a) the facts and circumstances of the business make electing the alternative suboptimal (e.g., because the entity may pursue an initial public offering in the future and the financial statements included in the registration statement would not be allowed to reflect any PCC accounting alternative), or (b) the private company is unaware of the alternative.

Under current U.S. GAAP, a company that voluntarily adopts a new accounting principle for the first time after its effective date is required to justify that the new principle is preferable. Current guidance generally requires retrospective application of the new accounting principle when it is voluntarily adopted. Stakeholders were concerned that the preferability assessment and retrospective application would be significant disincentives for private companies to adopt PCC accounting alternatives after their effective dates.

## Key Provisions

The ASU applies to only the four PCC private company accounting alternatives. It would not apply to other private company alternatives in other FASB standards such as the option to omit the tax-rate reconciliation disclosure or segment disclosures.[3]

### Specialized Transition

The ASU also provides specialized transition provisions for adopting the goodwill amortization and simplified hedge accounting alternatives. Under previous accounting change guidance, a private company electing the goodwill amortization alternative for the first time after its effective date would have been required to apply the standard retrospectively. The PCC concluded that this could be costly and diminish the relief that the alternative offers. To address this concern, the ASU requires prospective application of the goodwill alternative on adoption, regardless of when the entity adopts the ASU.

Additionally, a private company that elects the simplified hedge accounting approach for the first time after its effective date generally would have been unable to apply it to existing swaps. Typically, these contracts would not have a fair value at or near zero after inception and would not meet all of the criteria required to apply the PCC alternative (absent specialized transition). Because this inability would limit the benefit of the alternative, the ASU allows a private company to elect the simplified hedge accounting approach for existing swaps on adoption of the alternative if the specialized transition criteria are met, regardless of when adoption takes place. One specialized criterion is that the fair value of the existing swap does not need to be at or near zero at the time simplified hedge accounting is adopted if fair value was at or near zero when the entity entered into or acquired the swap.

[3] FASB ASC paragraphs 740-10-50-13 and 280-10-15-3, available at www.fasb.org.

However, if the private company does not apply the simplified approach to existing swaps at adoption and applies it for only newly executed contracts, the entity would be precluded from later applying the approach to those existing swaps.

The transition guidance also was extended indefinitely for the common control leasing alternative and the identifiable intangible asset alternative. However, the transition to those alternatives is simpler and would have been the same regardless of when they were adopted even if the Board had not addressed transition in this ASU. Common control leasing requires retrospective transition. The identifiable intangible assets alternative is applied to the first business combination that takes place in the annual period of adoption of the alternative.

## Effective Date and Disclosures

The ASU is effective immediately, which allows a private company to adopt, for the first time, any of the four private company accounting alternatives as of the beginning of:

- Its 2015 annual reporting period (or prior annual reporting periods) as long as those annual financial statements have not yet been made available for issuance; or
- Any subsequent annual period.

While the ASU does not require incremental disclosures, private companies still need to follow current U.S. GAAP disclosure requirements for changes in accounting principles.[4]

**Contact us:** This is a publication of KPMG's Department of Professional Practice 212-909-5600

**Contributing authors:** Paul H. Munter, Angela B. Storm, and Brandon I. Kano

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[4] FASB ASC paragraph 250-10-50-1, available at www.fasb.org.