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Private Companies Rejoice - VIE Rules are Changing for the Better

FINANCIAL SERVICES
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The Financial Accounting Standards Board (FASB) recently released one of the most anticipated changes to accounting guidance for variable interest entities (VIE). The change is intended to provide relief to private companies from challenges that have arisen from going through the evaluation and the potential consolidation of these entities, as well as to eliminate diversity in practice in the accounting for and disclosure of involvement with VIEs. This new accounting guidance does not change the existing voting interest model and will continue to require consolidation of an entity that another entity controls.

This guidance permits private entities to make an accounting policy election to forgo consolidation of entities that had complex common control arrangements, which usually resulted in them being a VIE of an entity, despite lack of control in that entity. The expectation is that if an entity makes the policy election, there will be significantly fewer VIEs consolidated by private companies.

These changes will require significant disclosure about the involvement with VIEs under common control, but are similar to existing related party disclosures and would include elements such as risks, assets and liabilities associated with the involvement in the VIE, guarantees and other significant contractual items.

Private companies have the ability to early-adopt these changes immediately or wait until the fiscal years beginning after December 15, 2019. When implementing the change, private companies will need to apply this change retrospectively and employ a cumulative adjustment to retained earnings in the earliest period presented.

Private companies, therefore, should start evaluating their VIEs now and decide if they meet the definition of being under common control to determine if they can be deconsolidated or if further analysis is required. Also remember to evaluate the impact of deconsolidating any VIE on the entity’s debt, lease or other significant contractual agreements. Proactive discussions with the users of the entity’s financial statements will help in understanding the reason for the accounting policy change.

While the effort will be quite a bit work in year one, it could greatly simplify an entity’s financial statements on a go-forward basis.

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