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Summary

The FASB issued ASU 2022-02[1] ("ASU") to eliminate the troubled debt restructuring (TDR) accounting model in ASC 310-40 for creditors that have adopted the guidance on measurement of credit losses in ASU 2016-13[2] (ASC 326) and require public business entities to disclose current-period gross writeoffs by year of origination for financing receivables and net investments in leases. The final ASU is available here. It is effective for years beginning after December 15, 2022 for entities that have adopted CECL. Otherwise, the ASU is effective when an entity adopts CECL.

Background

ASC 310-40[3] currently provides an exception to the general recognition and measurement guidance for loan restructurings and refinancings that meet specific criteria to be considered a TDR. In accordance with ASC 326, if a modification is a TDR, an incremental expected loss, if any, is recorded in the allowance for credit losses upon modification. Additionally, specific disclosures

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Credit Loss ("CECL") model in Topic 326. In addition, preparers indicated the cost and complexity of determining whether a modification represents a TDR and measuring its effect on the allowance for credit losses is high.

Additionally, users noted that designating a loan as a TDR generally does not affect their analyses of an entity's financial performance. Therefore, the FASB decided to eliminate the TDR recognition and measurement guidance for creditors that have already adopted CECL and enhance the disclosure requirements for modifications of receivables to debtors experiencing financial difficulty.

The FASB also clarified the existing vintage disclosure guidance for public business entities, as noted below.

Main Provisions

- The TDR accounting model in ASC 310-40 is eliminated for creditors that have adopted ASU 2016-13.
- Creditors should evaluate all modifications as either a new loan or the continuation of an existing loan under the general guidance on loan refinancing and restructuring in ASC 310-20-35-9 through 35-11.
- The ASU clarifies that for disclosure purposes, the term 'modification' includes principal forgiveness, interest rate reduction, other-than-insignificant payment delays, term extensions, or any combination thereof. Covenant waivers and modifications of contingent acceleration clauses (e.g. contingent call option) are not considered as term extensions.
- For disclosure purposes, the objective is to inform users as to the types and magnitude of modifications and the creditor's success in mitigating potential credit losses through the modifications. Specific disclosure requirements include:
    - For each reporting period where a statement of income is presented, creditors should disclose the following information for modifications of receivables to borrowers experiencing financial difficulty:
        - By class of financing receivable, qualitative and quantitative information about:
            1. The types of modifications utilized by an entity.

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4. The financial effect of the modification by type of modification, including the changes to the contractual terms as a result of the modification and the incremental effect of principal forgiveness on the amortized cost basis of the modified receivables, or the reduction in weighted-average interest rates for interest rate reductions.

5. Receivable performance in the 12 months after a modification.

- By portfolio segment, qualitative information on how the entity factored those modifications and the debtor's subsequent performance into the allowance for credit losses.

- For each reporting period where a statement of income is presented, creditors should disclose the following information about financing receivables that had a payment default during the period and had been modified within the 12 months preceding the payment default when the debtor was experiencing financial difficulty at the time of the modification:

  - By class of financing receivable, qualitative and quantitative information about:

    1. The type of contractual change that the modification provided

    2. The amount that defaulted, including the period-end amortized cost basis that defaulted.

  - By portfolio segment, qualitative information on how the entity factored those defaults into the allowance for credit losses.

- As a practical expedient, an entity may exclude the accrued interest receivable balance that is included in the amortized cost basis for the purposes of the disclosure requirements in ASC 326-20.

- If an entity modifies the same receivable in more than one manner (e.g., forgiveness of principal combined with an interest rate reduction), it should disclose sufficient information for users to understand the different types of modifications provided to borrowers. This may include, for example, presenting amortized cost basis of a receivable in separate categories that reflect the combination of modifications granted.

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Effective Dates and Transition

For entities that have adopted the amendments in ASU 2016-13, the amendments are effective for fiscal years beginning after December 15, 2022, including interim periods within those fiscal years. For entities that have not yet adopted the amendments in ASU 2016-13, the effective dates are the same as the effective dates in ASU 2016-13.

Early adoption of the amendments in this Update is permitted if an entity has adopted the amendments in Update 2016-13, including adoption in an interim period. If elected in an interim period, the guidance should be applied as of the beginning of the year. An entity may elect to early adopt the amendments about TDRs separately from the amendments related to vintage disclosures.

The amendments related to vintage disclosures should be applied prospectively. Entities may elect to apply the amendments related to recognition and measurement of TDRs either prospectively or on a modified-retrospective basis by recording a cumulative-effect adjustment to retained earnings in the period of adoption.

Have Questions? Contact Us

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[1] Financial Instruments—Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures.

[2] Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments.

[3] Receivables—Troubled Debt Restructurings for Creditors.

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