FASB FINANCIAL ACCOUNTING STANDARDS BOARD

Board Meeting Handout

Codification Improvements: Financial Instruments—Credit Losses (Vintage Disclose: Gross Writeoffs and Gross Recoveries)

February 2, 2022

Meeting Purpose

1. The Board will discuss redeliberation issues arising from comment letters received from stakeholders on the proposed Accounting Standards Update, *Financial Instruments—Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures,* benefits and costs of the proposed amendments, and whether to proceed to drafting a final Update for vote by written ballot.

Questions for the Board
1. Does the Board want to affirm its decision to require gross writeoff by year of origination? If so, does it want to affirm its decision to require only current-period gross writeoffs?
2. Does the Board want to affirm its decision to not require gross recoveries by year of origination in the vintage disclosure?
3. Does the Board want to affirm its decision to use a prospective transition approach and allow early adoption on a topic-by-topic basis? If so, does the Board want to make the amendments effective for fiscal years beginning after December 15, 2022?
4. Does the Board think that the expected benefits of the changes justify the perceived costs?
5. Does the Board direct the staff to draft a final Update for vote by written ballot?

Comment Letter Demographics

2. The proposed Update was issued for public comment on November 23, 2021, with a 30-day comment period. Feedback was due on December 23, 2021, and the table below describes the composition of stakeholders who provided feedback on the proposed Update. The proposed Update included provisions related to the Board's project to eliminate the recognition and measurement of troubled debt restructurings (TDRs) for creditors that have adopted current expected credit losses (CECL) model and the vintage

disclosure enhancements described further in this memo. Some comment letter respondents chose to comment only on the provisions related to the TDR project.

Type of Respondent	Number of Comment Letters	Number of Comment Letters—Commented on Vintage Disclosure Proposal
Practitioners	9	8
Public Preparers	10	9
Private Prepares	4	2
Trade Groups	7	3
Regulators	2	0
Total	**32**	**22**

3. In addition to the comment letter feedback received, there were two responses received during the Board's recent Invitation to Comment, *Agenda Consultation,* issued in June 2021 that discussed this project. Comments on that document were due in September 2021, which was before the issuance of the proposed Update. One comment letter was received from a global financial institution that also provided feedback on the proposed Update, and the specific feedback from that financial institution is included in the summary below. The other comment letter was received from a trade group focused on the securities industry encouraging the Board to consider the additional cost and anticipated effort as it relates to the corresponding benefit of providing gross writeoff and recovery information by year of origination.

Summary of Comments Received

General

4. Most stakeholders who commented on the vintage disclosure enhancements in the proposed Update supported the Board's decision to require current-period gross writeoffs by year of origination within the vintage disclosure. They supported the Board's decision to not require gross recovery information by year of origination or to require disclosure of cumulative writeoff or recovery information. Additionally, most stakeholders supported the transition provisions selected by the Board in deliberating the proposed Update. In addition, some stakeholders suggested clarifications to reduce potential diversity in practice upon applying the proposed Update.

Issue 1: Writeoffs

Background

5. The proposed Update would require that public business entities provide current-period gross writeoff information by year of origination within the vintage disclosure. This is consistent with one of the lines in Example 15 (paragraph 326-20-55-79) in Topic 326, Financial Instruments—Credit Losses. During the process of deliberating the proposed Update, the Board also considered whether to require cumulative gross writeoff information (rather than for the current period only).

Summary of Comment Letter Feedback

6. Fourteen comment letter respondents provided feedback about the requirement in the proposed Update to provide disclosure of current-period gross writeoffs. Of those respondents, nearly all supported the Board's decision and commended the Board for limiting the required information to only the information that financial statement users found to be most critical. In addition, all indicated that it would be significantly more burdensome to provide cumulative gross writeoff information by year of origination. Also, several respondents commented that that cumulative gross writeoff information by year of origination would not provide financial statement users with decision-useful information.

7. Preparers commented that the requirement would be operable and that the requirements were clear and understandable in the proposed Update, although there would be an initial set-up cost to make system changes to be able to provide the required information and design internal controls around the disclosure requirement as well. In addition, practitioners commented that the information would be auditable.

Alternatives

8. The Board will consider the following alternatives:

    (a) Alternative A: Affirm the Board's decision to require current-period gross writeoffs by year of origination within the vintage disclosure.

    (b) Alternative B: Require disclosure of cumulative gross writeoffs by year of origination within the vintage disclosure.

    (c) Alternative C: Do not require the disclosure of gross writeoffs by year of origination (cumulative or current period) within the vintage disclosure.

Issue 2: Recoveries

Background

9. Example 15 in Topic 326 (paragraph 326-20-55-79) includes both current-period gross writeoffs and gross recoveries. After the issuance of Accounting Standards Update No. 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments,* including during transition resource group meetings in 2017 and 2018 and subsequent discussion with financial statement users, feedback was received that both writeoff and recovery information would be important for financial statement users' analyses. In performing outreach with financial statement users as part of deliberations on the proposed Update, the staff heard feedback that while recovery information by year of origination could be useful, it was less critical than information about gross writeoffs and that it could be operably burdensome to provide.

10. On the basis of the feedback received, the Board decided not to require the disclosure of gross recoveries by year of origination in the proposed Update but asked a question in the proposed Update to determine if it was necessary information for financial statement users.

Summary of Comment Letter Feedback

11. Ten comment letter respondents commented on providing gross recovery information by year of origination. All of those comment letter respondents indicated that they supported the Board's decision to *not* require disclosure of gross recoveries by year of origination. The information received was largely consistent with the feedback received through the post-implementation review process and during project outreach.

12. Preparers continued to express concern about the operable complexities about providing this information and whether it would provide investors with decision-useful information. One practitioner cited potential audit complexities about the requirement to disclose gross recovery information by year of origination.

Alternatives

13. The Board will consider the following alternatives:

    (a) Alternative A: Affirm the Board's decision to not require gross recoveries by year of origination within the vintage disclosure.

    (b) Alternative B: Require gross recovery information by year of origination within the vintage disclosure.

Issue 3: Transition and Effective Date

Background

14. The proposed Update provides for a prospective transition methodology. That is, beginning in the period of adoption, an entity would provide current-period gross writeoffs in the vintage disclosures. Disclosure would not be required for prior comparative periods.

15. The proposed Update included provisions related to the elimination of TDR recognition and measurement guidance for creditors that have adopted CECL and the vintage disclosure enhancements described in this memo. The amendments in the proposed Update would allow entities to early adopt the provisions on a topic-by-topic basis. That is, an entity could elect to early adopt the provisions related to TDR recognition and measurement and not early adopt the provisions related to vintage disclosures until the required effective date.

16. The Board did not specify an effective date and asked a question in the proposed Update about what the earliest date is that entities would be able to provide the disclosures in the proposed Update. Also, the Board clarified in the questions in the proposed Update that it also would consider different effective dates for the two topics. Said differently, the TDR provisions could be effective at an earlier or later date than the vintage disclosure enhancement provisions.

Summary of Comment Letter Feedback

17. Ten comment letter respondents provided feedback on the transition methodology and/or effective date of the proposed Update:

    a. Three respondents commented on the transition approach in the proposed Update. Each of those respondents supported the prospective transition approach. This is consistent with the feedback received during the process to collect information for deliberations on the proposed Update, which is that it would be challenging for preparers to provide gross writeoff information by year of origination retrospectively (for periods before the adoption of the proposed Update) because system changes may be needed to provide that information.

    b. Nine comment letter respondents provided feedback about the effective date and early adoption of the proposed Update. Each of the stakeholders who provided a specific effective date indicated that they could adopt the proposed Update for fiscal periods beginning after December 15, 2022 (that is, Q1 2023 for an entity with a calendar fiscal year-end). Stakeholders also generally supported the ability to early adopt the provisions, acknowledging that some entities may be able to provide the information earlier. Additionally, stakeholders generally supported the ability to early adopt the provisions of the proposed Update on a topic-by-topic basis.

FASB FINANCIAL ACCOUNTING STANDARDS BOARD

Board Meeting Handout

Financial Instruments—Credit Losses (Topic 326): Targeted Improvements to the Accounting for Troubled Debt Restructuring (TDR) for Creditors

February 2, 2022

Meeting Purpose

1. The Board will discuss redeliberation issues arising from feedback on the proposed Accounting Standards Update, *Financial Instruments—Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures*, benefits and costs of the proposed amendments, and whether to proceed to drafting a final Update for vote by written ballot.

Questions for the Board
1. Does the Board want to affirm its decision that all receivable modifications should be evaluated under the modification guidance in paragraphs 310-20-35-9 through 35-11? 2. Does the Board want to affirm its decision to remove the guidance that allows entities to consider renewals, modifications, and extensions that result from reasonably expected modifications made to borrowers experiencing financial difficulty in estimating the allowance for credit losses? 3. Does the Board want to affirm and clarify its intent that a discounted cash flow method is not required to estimate the allowance for credit losses for modifications of receivables made to borrowers experiencing financial difficulty? If so, does the Board also want to affirm and clarify that entities continuing to measure the allowance for credit losses using a discounted cash flow (DCF) model may use the post-modification effective interest rate? 4. Does the Board want to require disclosure of modifications of receivables made to borrowers experiencing financial difficulty regardless of the asset class of the modified receivable? 5. Does the Board want to require disclosure of all modifications of receivables made to borrowers experiencing financial difficulty or just a subset of those modifications? 6. Does the Board want to affirm its decision to carry forward the insignificant delay in payment guidance, including the requirement to consider cumulative modifications, or shorten the look-back period to 12 months for those modifications? 7. Does the Board want to affirm its decision to require the disclosure enhancements included in the proposed Update?

8. Does the Board want to affirm its decision to require prospective transition with an option for modified retrospective transition (a cumulative effect adjustment to retained earnings in the period of adoption) for the elimination of troubled debt restructuring (TDR) recognition and measurement guidance?

9. Does the Board want an effective date for fiscal years beginning after December 15, 2022, for entities that have adopted Update 2016-13 and allow early adoption on a topic-by-topic basis?

10. Does the Board think that the expected benefits of the changes justify the perceived costs?

11. Does the Board direct the staff to draft a final Update for vote by written ballot?

Comment Letter Demographics

2. The proposed Update was issued for public comment on November 23, 2021, with a 30-day comment period. Feedback was due on December 23, 2021, and the table below describes the composition of stakeholders who provided feedback on the proposed Update.

Type of Respondent	**Number of Comment Letters**
Practitioners	9
Public Preparers	10
Private Prepares	4
Trade Groups	7
Regulators	2
Total	**32**

3. In addition to the comment letter feedback received, five responses were received during the Board's recent Invitation to Comment, *Agenda Consultation,* issued in June 2021 that discussed this project. Feedback on that document was due in September 2021, which was before the proposed Update was issued. Five respondents provided feedback about this project (two practitioners, two global financial institutions, and one trade group that represents the banking industry). All five respondents broadly supported the project and the Board's efforts to remove TDR recognition and measurement guidance for entities that have adopted Update 2016-13.

Summary of Comments Received

General

4. Nearly all comment letter respondents supported the Board's efforts to eliminate the recognition and measurement of TDRs for entities that have adopted the current expected credit losses (CECL) model. The comment letter respondents who supported removing TDR

recognition and measurement for entities that have adopted CECL agreed with the Board's decision that the effect of most TDRs has already been captured in the allowance for credit losses because Update 2016-13 requires the estimate of lifetime expected credit losses. Therefore, TDR recognition and measurement no longer provides decision-useful information after the adoption of Update 2016-13.

5. Most comment letter respondents acknowledged that if TDR recognition and measurement guidance were eliminated, enhanced disclosures would be necessary to provide financial statement users with the information that they need. However, several respondents provided feedback about the operability of certain of the disclosures included in the proposed Update, the scope of modifications that would be included in the disclosures, and points that could be clarified before issuing a final Update.

TDR Recognition and Measurement for Creditors That Have Adopted CECL

6. As a basis for the amendments in the proposed Update, the Board decided to eliminate any recognition and measurement differences that existed between modifications that resulted in TDRs and all other modifications. Therefore, the amendments in the proposed Update would result in no recognition and measurement differences as it relates to the measurement of expected credit losses between modifications that would have been TDRs and all other modifications. Additionally, the amendments in the proposed Update would result in all modifications being measured consistently. That is, even those modifications that would require disclosure because they are made to borrowers experiencing financial difficulty would not have any unique measurement attributes.

7. Stakeholders raised certain points about the application of general modification guidance to modifications that would have been TDRs. Specifically, comment letter respondents provided feedback about the evaluation of whether these loans represent new loans or continuations of existing loans; whether entities should be able to consider extensions, modifications, or renewals made in modifications to borrowers experiencing financial difficulty in determining the life of an asset over which to evaluate expected credit losses; and the methodology and effective interest rate used to measure the allowance for credit losses on certain modified loans.

Issue 1A: Application of Modification Guidance

Background

8. The amendments in the proposed Update would eliminate TDR recognition and measurement guidance for creditors that have adopted CECL. Instead, all modifications would be subject to the current guidance for loan restructurings and refinancings in

paragraphs 310-20-35-9 through 35-11 to determine if the modification represents a new loan or a continuation of the existing loan. To be considered a new loan, both of the following conditions must be met:

(a) The terms of the restructuring must be considered at least as favorable to the lender as terms for a comparable loan to other customers with similar collection risk.

(b) The modification is more than minor, which typically requires a comparison of cash flows between the original and modified loan to determine if the difference is greater than 10 percent.

9. The Board asked a question in the proposed Update to gather stakeholder feedback about whether the treatment of modifications in the proposed Update would yield meaningful financial statement outcomes and if the application of modification guidance for loans previously accounted for as TDRs is appropriate.

Comment Letter Feedback

10. Eighteen comment letter respondents provided feedback about the application of the modification guidance in paragraphs 310-20-35-9 through 35-11. Mixed feedback was received about the application of modification guidance for loans that would have been considered TDRs under current GAAP.

(a) Several stakeholders supported the application of modification guidance to all receivables within the scope of Topic 326, Financial Instruments—Credit Losses, including those that would have been TDRs under current GAAP.

(b) Other stakeholders noted that all modifications that would have been TDRs should be treated as continuations of the existing loan (and therefore not subject to evaluation under the modification guidance).

11. Several respondents described potential challenges that private entities may encounter in applying the modification guidance to modifications that currently would be considered TDRs.

12. Some practitioners recommended clarifying the current modification guidance to make it easier to apply.

Alternatives

13. The Board will consider the following alternatives:

(a) Alternative A: Affirm the Board's decision that all receivables should be evaluated under the modification guidance in paragraphs 310-20-35-9 through 35-11.

(b) Alternative B: Treat all modifications of receivables to borrowers experiencing financial difficulty as continuations of the existing loan.

Issue 1B: Contractual Life—Reasonably Expected TDRs

Background

14. Update 2016-13 requires that an entity estimate expected credit losses over the contractual term of a financial asset. The CECL model captures the life of a specific asset rather than the life of a lending relationship. As a result, the guidance in paragraph 326-20-30-6 does not allow an entity to consider expected extensions, renewals, and modifications in determining the contractual term of the asset over which to estimate credit losses *unless* the entity has a reasonable expectation at the reporting date that it will execute a TDR with the borrower (reasonably expected TDR).

15. From limited outreach performed as part of this project, the staff understands that some entities have determined that the effect of reasonably expected TDRs is not significant in determining the allowance for credit losses.

16. The amendments in the proposed Update would remove the guidance in paragraph 326-20-30-6 that allows an entity to consider reasonably expected TDRs in determining the life of an asset over which to estimate expected credit losses. That is, an entity would be precluded from considering *all* expected extensions, renewals, and modifications (except as provided in paragraph 326-20-30-6(b)) in determining the life of the asset over which to estimate the allowance for credit losses.

Comment Letter Feedback

17. A few comment letters addressed the Board's proposal to remove the guidance in paragraph 326-20-30-6 that allows entities to extend the contractual term for reasonably expected TDRs, most of which suggested retaining the ability to consider extensions, renewals, and modifications for loans reasonably expected to be modified to borrowers experiencing financial difficulty. Comment letter respondents explained that removing this guidance may result in a measurement of credit losses that is inconsistent with a lender's risk management strategies and that does not depict the actual amount of credit losses that an entity would expect to occur. Additionally, a few stakeholders raised concern that removing the guidance would suggest that historic loss experience that factors in extensions, renewals, or modifications would have to be adjusted to remove those actions, which would be burdensome and also would not accurately depict expected credit losses.

18. One stakeholder provided an example in its comment letter about the effect of removing the guidance. The example assumes that a lender has a commercial real estate development loan scheduled to mature in three months. However, the borrower is experiencing delays in completing the project because of supply chain issues and is experiencing financial difficulty related to a downturn in market conditions. The lender would expect to extend the term of the loan to allow the borrower ample time to get supplies to finish and sell the real estate project. However, the example indicates that if the lender could not consider an extension, it may suggest that the lender would have to foreclose on the property even though reflecting the foreclosure in its allowance for credit losses would not reveal the entity's loss mitigation strategy or the amount that it actually expects to collect.

Alternatives

19. The Board will consider the following alternatives:

(a) Alternative A: Affirm the Board's decision to remove the guidance that allows entities to consider renewals, modifications, and extensions in estimating the allowance for credit losses as a result of reasonably expected modifications made to borrowers experiencing financial difficulty.

(b) Alternative B: Retain the guidance that allows entities to consider renewals, modifications, and extensions for reasonably expected TDRs in estimating the allowance for credit losses but amend it to apply to modifications made to borrowers experiencing financial difficulty.

Issue 1C: DCF Model and Effective Interest Rate

Background

20. At its September 6, 2017 meeting, the Board indicated that for loans modified in a TDR in which the effect of the concession could be measured only using a DCF model or reconcilable method, the DCF or reconcilable method should be used to measure the allowance for credit losses on those loans. As a result, entities frequently measure the allowance for credit losses on loans modified in a TDR using a DCF model because the effect of some common concessions, such as interest rate concessions or term extensions, can be captured only using a DCF model.

21. Under current GAAP, paragraph 310-40-35-12 requires that the effective interest rate in a DCF model be based on the original contractual interest rate of a loan modified in a TDR rather than a post-modification contractual interest rate. Paragraph 326-20-30-4A allows entities to elect, by class of financing receivable, to adjust the effective interest rate used in

a DCF to consider timing and changes in timing of expected cash flows unless the asset is restructured in a TDR, in which case the effective interest rate cannot be adjusted.

22. The guidance in paragraphs 310-40-35-12 and 326-20-30-4A requires that an entity use an effective interest rate based on pre-modification contractual interest rates so that the effect of any TDR modification is captured in the allowance for credit losses using a DCF model. That is because if the denominator (effective interest rate) were updated to reflect changes in terms after the TDR modification, it would offset any changes to the amount or timing of cash flows associated with the loan and, therefore, the allowance for credit losses would not fully capture the concession.

23. Paragraph BC22 of the proposed Update, which was included to indicate that if an entity intends to continue using a DCF model after the adoption of the proposed amendments, it would be inappropriate to ignore the fact that a modification has been made.

24. The proposed Update would supersede Subtopic 310-40, Receivables—Troubled Debt Restructurings by Creditors, in its entirety. Therefore, the guidance in paragraph 310-40-35-12 that precludes an entity from changing the effective interest rate in a loan modified as a TDR would no longer be in GAAP. The amendments in the proposed Update also would change paragraph 326-20-30-4A such that the guidance would no longer preclude an entity from making an election to adjust the effective interest rate for timing and changes in timing of expected cash flows when using a DCF model. The effect of the change to those two paragraphs in the proposed Update is that there no longer would be guidance in GAAP that would preclude an entity from updating the effective interest rate when using a DCF model.

Comment Letter Feedback

25. Several comment letter respondents requested that the Board clarify the meaning of paragraph BC22 as it relates to an entity’s continued use of a DCF model after adopting a final Update of these proposed amendments. Some comment letter respondents interpreted paragraph BC22 as requiring the continued use of a DCF model after adopting the proposed Update or modifications of receivables to borrowers experiencing financial difficulty.

Alternatives

26. The Board will consider the following alternatives:

    (a) Alternative A: Affirm and clarify the Board’s intent that a DCF model not be required for modifications of receivables made to borrowers experiencing financial difficulty and that the post-modification effective interest rate may be used by entities that continue to measure the allowance for credit losses using a DCF model.

(b) Alternative B: Require that a DCF model or reconcilable method be used to measure the allowance for credit losses for modifications of assets made to borrowers experiencing financial difficulty and retain the guidance in paragraph 326-20-30-4A and similar guidance about what is included in Subtopic 310-40 that requires using the pre-modification effective interest rate.

Issue 2A: Disclosure Scope—Asset Class

Background

27. The proposed Update did not explicitly state which assets were within the scope of the disclosure enhancements. Some stakeholders understood that because the disclosure enhancements in the proposed Update were included in Subtopic 310-10, the disclosure enhancements would apply to all modifications of financial assets within the scope of Topic 310 to borrowers experiencing financial difficulty, including trade accounts receivable, loans, loan syndications, factoring arrangements, standby letters of credit, and financing receivables. However, the proposed Update included a question about whether there are any assets within the scope of Topic 326 that should not be subject to the enhanced disclosure requirements in the proposed Update. Certain assets that are within the scope of Topic 326 are not within the scope of Subtopic 310-10, such as net investments in leases and held-to-maturity debt securities.

Summary of Comment Letter Feedback

28. Seven comment letter respondents provided feedback about asset classes of receivables that should or should not be subject to the proposed disclosure enhancements.

29. Some practitioners supported applying the disclosure enhancements to all assets within the scope of Topic 326. One practitioner suggested that the disclosures may not be decision useful for receivables that are a by-product of other transactions, such as revenue contracts with customers and reinsurance activities. One practitioner opposed requiring the disclosures for acquired receivables that at acquisition had more than insignificant deterioration since origination.

30. Three comment letter respondents commented on the disclosure enhancements as they relate to lease modifications within the scope of Topic 842, Leases. One of those respondents noted that the legacy guidance would not require TDR disclosure for lease modifications and indicated that it was unclear if it was the Board's intent to require the disclosure enhancements in the proposed Update for those modifications. The other two

comment letter respondents explicitly stated that the disclosure enhancements should not apply to lease modifications within the scope of Topic 842.

Alternatives

31. The Board will consider the following alternatives:

    (a) Alternative A: Require disclosure of modifications of receivables made to borrowers experiencing financial difficulty regardless of the asset class of the modified receivable for all assets within the scope of Subtopic 310-10.

    (b) Alternative B: Require disclosure of modifications of receivables made to borrowers experiencing financial difficulty regardless of the asset class of the modified receivable for all assets within the scope of Subtopic 326-20.

Issue 2B: Disclosure Scope—Modification Type

Background

32. The amendments in the proposed Update would require that the disclosure enhancements be provided for all modifications of receivables made to borrowers experiencing financial difficulty. Current GAAP requires that all modifications made to borrowers experiencing financial difficulty that also involve the lender extending a concession be accounted for as TDRs. Therefore, the population of modifications that require disclosure under the proposed Update is broader than those modifications that were previously considered to be TDRs and, therefore, subject to the TDR disclosure requirements.

Comment Letter Feedback

33. Sixteen comment letter respondents discussed the types of modifications that should be subject to the disclosure enhancements in the proposed Updates. All of the stakeholders who provided feedback on this topic were preparers or trade groups (with the exception of one practitioner). Most of those comment letter respondents indicated that the scope of the types of modifications that would be included in the disclosure enhancements is too broad.

34. Several stakeholders suggested that in order to more effectively provide information about modifications made to borrowers experiencing financial difficulty that would actually change an entity's credit risk profile for an asset, the disclosures should be limited to modifications that change the amount or timing of cash flows associated with a loan.

Alternatives

35. The Board will consider the following alternatives:

(a) Alternative A: Affirm the Board's decision to require disclosure of all modifications made to borrowers experiencing financial difficulty.

(b) Alternative B: Require disclosure of modifications that result in a direct change in the timing or amount of contractual cash flows to borrowers experiencing financial difficulty.

(c) Alternative C: Require disclosure of modifications that are concessions to borrowers experiencing financial difficulty.

Issue 2C: Disclosure Scope—Insignificant Delay in Payment

Background

36. The amendments in the proposed Update would exclude modifications that result only in a delay in payment that is insignificant from the modification disclosure requirements in paragraphs 310-10-50-36 and 310-10-50-40 through 50-42. Under current GAAP, insignificant delays of payment are not considered to be concessions and therefore are not considered to be TDRs.

37. Under current GAAP, when considering whether a delay in payment is insignificant (and therefore does not represent a concession), entities are required to consider the cumulative effect of all previous modifications. The requirement to consider cumulative past modifications was carried forward in the proposed Update. Therefore, an entity would be required to consider previous modifications when determining whether a delay in payment is insignificant and, therefore, does not have to be included in the enhanced disclosure requirements for modifications made to borrowers experiencing financial difficulty.

Comment Letter Feedback

38. Thirteen respondents provided feedback about the Board's decision to carry forward the insignificant delay in payment guidance. All but one of those respondents supported the Board's decision to carry forward the guidance from Subtopic 310-40 into the amendments in the proposed Update and to exclude those insignificant modifications from the enhanced disclosures. However, many of those stakeholders commented that the requirement to consider cumulative modifications when determining if a delay in payment is insignificant could be operably burdensome and may not provide financial statement users with decision-useful information to financial statement.

39. Comment letter respondents recommended that the Board consider limiting the previous modifications "lookback" period to a specific period (rather than just requiring general cumulative consideration over the entire life). Stakeholders noted that for borrowers,

guidance about determining whether a loan modification represents a modification or extinguishment only considers previous modifications made in the previous 12-month period and suggested that a similar 12-month lookback period be considered for previous modifications when determining whether a modification represents an insignificant delay in payment.

Alternatives

40. The Board will consider the following alternatives:

    (a) Alternative A: Affirm the Board's decision to carry forward the insignificant delay in payment guidance, including the requirement to consider cumulative modifications.

    (b) Alternative B: Carry forward the insignificant delay in payment guidance, but only require that an entity look back at modifications made in the previous 12-month period.

Issue 2D: Disclosure Enhancements

Background

41. The proposed Update included enhanced disclosure requirements to be provided about modifications of receivables made to borrowers experiencing financial difficulty.

42. In addition, the proposed Update included a disclosure objective to guide entities in providing financial statement users with decision-useful information about modifications of receivables made to borrowers experiencing financial difficulty, as well as other modifications that it otherwise may provide voluntary disclosure about.

Comment Letter Feedback

43. Twenty-two comment letter respondents provided commentary about the disclosure enhancements in the proposed Update. In general, most comment letter respondents supported some of the disclosure enhancements. That is, in lieu of TDR recognition and measurement, as well as the specific disclosure requirements currently in place for TDRs, most stakeholders understood the need to revisit and enhance disclosure requirements for certain modifications. However, some stakeholders had mixed feedback about the operability of certain of the disclosures or suggested clarifications to some of the disclosure requirements.

44. In addition to the general disclosures described above, there were two aspects of the proposed disclosures that several stakeholders commented on:

(a) Five stakeholders commented on the requirement in paragraph 310-10-50-40(a)(1) in the proposed Update to disclose the pre-modification amortized cost basis of modified receivables made to borrowers experiencing financial difficulty during the reporting period. Those stakeholders acknowledged that it would be difficult to produce this information because they would have to take a "snapshot" of a loan at a particular point in time and making system changes and implementing controls to do so could be challenging. They also commented that pre-modification amortized cost basis (ACB) is inconsistent with disclosing the percent of total ACB of a particular class of financing receivable, which would be based on the amount at the reporting date, rather than at the modification date. As a result, they suggested that the Board require the disclosure of the end-of-period amortized cost basis of the modified receivable.

(b) Four stakeholders provided feedback about the requirement in paragraph 310-10-50-41 in the proposed Update to include receivables that have been modified in multiple ways during the reporting period to be included in a separate "combination" column. Those stakeholders acknowledged that for some entities a majority of modifications involve a combination of modification types and, therefore, aggregating all of this information into one "combination" column may not provide financial statement users with transparent information.

Alternatives

45. The Board will consider the following alternatives:

(a) Alternative A: Affirm the Board's decision on the disclosure enhancements included in the proposed Update.

(b) Alternative B: Make certain edits to the disclosure requirements in the proposed Update, including changing the guidance in paragraph 310-10-50-40(a)(1) to require disclosure of period-end amortized cost basis and permit greater disaggregation of the "combination" column required in paragraph 310-10-50-41, while affirming the Board's decision on the other aspects of the disclosure enhancements.

(c) Alternative C: Separate the disclosure enhancement piece of the project and consider it as a separate project.

Issue 3A: Transition Methodology

Background

46. The amendments in the proposed Update called for a prospective transition methodology for disclosures. In the period of adoption, entities would provide the required disclosures for the current period; all comparative periods included in financial statements before the date of adoption would provide legacy TDR disclosures.

47. As it relates to the elimination of the recognition and measurement guidance for TDRs, the proposed transition approach would require a prospective transition whereby all modifications made after the adoption of a final Update would be subject to the modification guidance in paragraphs 310-20-35-9 through 35-11. For all modifications previously made that were considered to be TDRs, the allowance for credit losses would continue to be measured and accounted for using the current TDR guidance in Subtopic 310-40. However, the proposed guidance also would provide entities with an option to apply the guidance on a modified retrospective basis whereby any modifications previously classified as TDRs no longer would be recognized as such and any measurement differences in the allowance for credit losses would be reflected through a cumulative-effect adjustment to opening retained earnings in the period of adoption. The measurement difference represents the difference between the allowance for credit losses incorporating the modification that is a TDR and the method of measuring the allowance for credit losses after adoption of the proposed Update.

Comment Letter Feedback

48. Eighteen comment letter respondents provided feedback on the transition approaches in the proposed Update.

49. Many comment letter respondents indicated that they supported the prospective transition approach as it relates to providing the required disclosure in the proposed Update and the options provided for the transition approach as it relates to recognition and measurement changes for TDRs.

50. A few stakeholders commented that transition should instead be treated as a change in accounting estimate or that the effect of adoption should flow through current period earnings upon adoption.

Alternatives

51. The Board will consider the following alternatives:

    (a) Alternative A: Affirm the Board’s decision to require prospective transition for disclosures and prospective transition with an option for modified retrospective transition for TDR recognition and measurement changes.

(b) Alternative B: Affirm the Board's decision to require prospective transition for disclosures and treat changes in recognition and measurement as a result of the elimination of TDRs as a change in estimate.

Issue 3B: Effective Date and Early Adoption

Background

52. The proposed Update did not specify an adoption date. However, it indicated that entities would be able to early adopt the guidance in the proposed Update and could elect early adoption on a topic-by-topic basis. Said differently, an entity would be allowed to early adopt the provisions related to TDRs separately from the provisions in the proposed Update related to vintage disclosure enhancements. The proposed Update can be adopted only by entities that have adopted Update 2016-13.

53. The Board asked comment letter respondents to provide feedback about the earliest date that the recognition and measurement changes and disclosure amendments in the proposed Update could be adopted.

Comment Letter Feedback

54. Comment letter respondents who responded to the question about the earliest date that their entity could adopt the proposed Update indicated that they would be able to adopt the provisions of the proposed Update related to TDRs for the fiscal year beginning after December 15, 2022. Early adoption was generally favored by stakeholders.

Board Meeting Handout

Financial Instruments—Credit Losses (Topic 326)—Acquired Financial Assets

February 2, 2022

Meeting Purpose

1. The Board will deliberate the accounting for acquired financial assets that are within the scope of Accounting Standards Update No. 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. Currently, the scope of the project is to expand the purchased credit-deteriorated (PCD) accounting model to all loans acquired in a business combination and to modify the presentation of expected credit losses for financial assets that meet the definition of PCD.

2. The staff will ask the Board to determine whether the accounting model for PCD assets should be expanded and, if so, to which assets and transactions.

Questions for the Board
Issue 1: Should There Be a Distinction between PCD and Non-PCD Assets and, If So, How Should It Be Determined? 1. Does the Board want to amend the accounting for acquired asset accounting to eliminate the "more than insignificant" test? **Issue 2: Which Model Should Be Applied to Acquired Assets?** 2. If the Board selects Alternative A in Question 1, which model would the Board like to apply for acquired assets? **Issue 3: Should Certain Asset Classes Be Excluded?** 3A. Does the Board want to exclude certain credit card receivables and other revolving lending arrangements from applying the acquisition model of accounting (PCD accounting model)? 3B. Does the Board want to exclude available-for-sale (AFS) debt securities from applying the acquisition model of accounting (PCD accounting model)? 3C. Does the Board want to exclude assets that are not recognized at fair value from applying the acquisition model of accounting (PCD accounting model)?

The staff prepares Board meeting handouts to facilitate the audience's understanding of the issues to be addressed at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect the views of the FASB or its staff. Official positions of the FASB are determined only after extensive due process and deliberations.

4. Does the Board want to clarify that contract assets acquired in a business combination should be treated as an originated asset (non-PCD accounting model)?

Issue 4: Should Assets Acquired in Business Combinations and Asset Acquisitions Be Treated Consistently?

5. Does the Board want to limit the application of the acquisition model of accounting to acquired assets recognized in a business combination only?

Issue 5: Seasoning

6. Does the Board want to incorporate "seasoning" into the acquisition model of accounting?

7. Does the Board have any initial leanings on how to define *seasoning*?

8. Does the Board want to consider incorporating a difference between contractual and expected cash flows into the definition of *seasoning*?

Background

3. At the July 14, 2021 Board meeting, the Board added a project to its technical agenda to address the accounting for acquired financial assets in accordance with Update 2016-13. The Board added a project to consider expanding the scope of the PCD accounting model to all loans acquired in a business combination and to consider modifying the presentation of expected credit losses for acquired financial assets that meet the definition of PCD.

4. The Board also directed the staff to perform additional research and outreach related to the accounting for acquired financial assets, including:

   (a) A potential scope expansion to apply PCD accounting to other financial assets (not just loans) acquired in a business combination and/or all acquired seasoned loans, including loans acquired in an asset acquisition.

   (b) A potential scope reduction that would exclude debt securities, beneficial interests, and other revolving borrowing arrangements, trade accounts receivables, and other assets from the PCD accounting model.

   (c) A potential change in measurement that would base the allowance for credit losses on the purchase price (instead of par) for those assets applying PCD accounting.

Why Are Changes Being Proposed?

5. Since the issuance of Update 2016-13, the Board has received feedback from stakeholders that identified opportunities for improvement in the accounting model for acquired financial assets that are within the scope of Update 2016-13. That feedback has been received

primarily from financial statement users and preparers. Much of the feedback received from preparers focused on challenges encountered in explaining to investors the accounting for acquired assets within the scope of Update 2016-13. That is, several preparers who have had material acquisitions since the issuance of Update 2016-13 cited difficulty in educating investors and analysts about the effect of credit losses recorded on acquired financial assets.

6. The staff conducted outreach with financial statement users throughout 2020 and 2021 to gather feedback about their observations related to the acquired financial asset model in Update 2016-13. Generally, financial statement users noted that current acquired asset accounting was difficult to understand. Most of the user feedback was focused on the designation of certain financial assets as PCD or non-PCD at the acquisition date and the non-PCD accounting model. The staff heard consistent feedback from financial statement users that the current acquired asset accounting is complex and may not provide decision-useful information and that the non-PCD accounting model does not provide meaningful financial statement outcomes.

7. Following the July 14, 2021 Board meeting, the staff conducted additional outreach with investors and analysts, preparers, practitioners, and regulators to gather feedback on the issues related to the accounting for acquired financial assets within the scope of Topic 326.

8. In addition, there were three responses received during the Board's recent Invitation to Comment, *Agenda Consultation,* issued in June 2021 that discussed this project. All three respondents who commented on the project (one practitioner and two preparers that are global financial institutions) supported the Board's efforts as they relate to the project. One respondent (a global financial institution) commented that it supported the Board's recommendation to expand the PCD accounting model and specifically suggested applying the PCD accounting model to all acquired loans and held-to-maturity debt securities within the scope of Topic 326.

Issue 1: Should There Be a Distinction between PCD and Non-PCD Assets and, If So, How Should It Be Determined?

Alternatives

9. The Board will consider the following alternatives:

   (a) Alternative A: Amend current acquired asset accounting such that there is no longer a distinction between PCD and non-PCD assets upon acquisition.

   (b) Alternative B: Amend current acquired asset accounting by amending the threshold to determine whether an asset is PCD or non-PCD upon acquisition.

   (c) Alternative C: Do not amend current acquired asset accounting.

Issue 2: Which Model Should Be Applied to Acquired Assets?

10. If the Board selects Alternative A in Issue 1, it will need to determine which accounting model to apply to acquired assets upon acquisition. In determining which model to apply, the Board would effectively decide which accounting model (that is, the PCD accounting model or the non-PCD accounting model) would be applied "by default" to all acquired assets. The Board will have an opportunity in Issue 3 to determine if there are certain asset classes or types of transactions that should not follow the default model.

Alternatives

11. The staff believes that there are two feasible alternatives for the Board's consideration:

    (a) Alternative A: Apply the PCD accounting model for all acquired assets.

    (b) Alternative B: Apply the non-PCD accounting model for all acquired assets.

Issue 3: Exclusion of Certain Asset Classes

12. The Board may determine that applying the PCD accounting model to certain asset classes or types of transactions would be operably burdensome or not provide financial statement users with appropriate information. In that case, the Board may decide that upon acquisition, those assets should be treated as originations. Said differently, if the Board's decisions in Issues 1 and 2 result in all acquired assets applying the PCD accounting model, the Board may choose to create exceptions to applying the default model. If the Board identifies an exception, that asset class or transaction type would apply the current non-PCD accounting model (which is akin to an origination).

Credit Cards

13. The Board will consider the following alternatives:

    (a) Alternative A: Credit cards and other revolving lending arrangements would apply the PCD accounting model.

    (b) Alternative B: Only credit cards and other revolving lending arrangements in which the borrower has active borrowing privileges would not apply the PCD accounting model (they would apply the origination (non-PCD) model).

    (c) Alternative C: Credit cards and other revolving lending arrangements would not apply the PCD accounting model (they would apply the origination (non-PCD) model).

AFS Debt Securities

14. The Board will consider the following alternatives:

    (a) Alternative A: AFS debt securities would apply the PCD accounting model.

    (b) Alternative B: AFS debt securities would not apply the PCD accounting model.

Assets Not Acquired at Fair Value Upon Acquisition

15. The Board will consider the following alternatives:

    (a) Alternative A: Assets that are not recognized at fair value upon acquisition would apply the PCD accounting model.

    (b) Alternative B: Assets that are not recognized at fair value upon acquisition would not apply the PCD accounting model.

Contract Assets

16. The Board will consider whether to clarify that contract assets resulting from transactions with customers acquired in a business combination should follow the non-PCD accounting model.

Issue 4: Should Assets Acquired in Business Combinations and Asset Acquisitions Be Treated Consistently?

17. The Board will consider the following alternatives:

    (a) Alternative A: Account for assets acquired in a business combination using the PCD accounting model.

    (b) Alternative B: Account for all acquired assets using the PCD accounting model.

Issue 5: Seasoning

18. If the Board decides to incorporate seasoning for asset acquisitions, the staff will come back to the Board with further research and fully developed alternatives to define *seasoning* at a future meeting. To help focus the staff's research in this area, the staff would like to understand the Board's initial leanings regarding how to define *seasoning*. The Board will consider the following alternatives:

    (a) Alternative A: Principles-based definition of *seasoning*

    (b) Alternative B: Bright-line threshold to define *seasoning*

    (c) Alternative C: Combination of principles-based and bright-line definition of *seasoning*.

Additional Seasoning Consideration: Contractual versus Expected Cash Flows

19. In February 2018, Credit Acceptance Corporation submitted an agenda request to consider whether certain assets that the company acquires could apply the PCD model. The specific request asked the Board to consider whether the PCD model could be applied "by analogy" to those assets that otherwise would not qualify for the PCD model.

20. The Board will consider whether to incorporate into the concept of "seasoning" a consideration of whether there is a significant difference between contractual and expected cash flows on an asset, regardless of how "old" the asset is. Said differently, the Board could make the seasoning assessment a two-prong test by defining *seasoning* as either (a) loans that have not been recently originated or (b) loans that have a significant difference between expected and contractual cash flows.

Board Meeting Handout

Accounting Standards Update No. 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*

February 2, 2022

Meeting Purpose

1. The Board will discuss agenda request letters submitted by stakeholders requesting the deferral of the effective date of the current expected credit losses (CECL) model for nonpublic entities.

Questions for the board
1. Does the Board want to add a project to its agenda to defer the effective date of CECL for nonpublic entities? *Alternative A*: Do not defer the effective date of CECL for nonpublic entities. *Alternative B*: Defer the effective date of CECL for nonpublic entities by one year, to fiscal years beginning after December 15, 2023, including interim periods within those years. *Alternative C*: Indefinitely defer the effective date of CECL for nonpublic entities, excluding smaller reporting companies, with early application permitted.

2. The Board issued Update 2016-13 in June 2016. The original effective dates were as follows:

   (a) For public business entities that meet the definition of a Securities and Exchange Commission (SEC) filer, for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years.

   (b) For public business entities that do not meet the definition of an SEC filer, for fiscal years beginning after December 15, 2020, including interim periods within those fiscal years.

(c) For all other entities, including not-for-profit entities and employee benefit plans within the scope of Topics 960 through 965 on plan accounting, for fiscal years beginning after December 15, 2020, and interim periods within fiscal years beginning after December 15, 2021.

3. Following the issuance of Update 2016-13, subsequent Accounting Standards Updates deferred the effective date of the Update as follows:

   (a) For public business entities that meet the definition of a SEC filer, excluding entities eligible to be smaller reporting companies as defined by the SEC, for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years.

   (b) For all other entities, for fiscal years beginning after December 15, 2022, including interim periods within those fiscal years.

4. In November 2018, the Board issued Accounting Standards Update No. 2018-19, *Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* which amended the effective date of CECL for nonpublic entities to annual and interim reporting periods beginning after December 15, 2021. Update 2018-19 was released to clarify the Board's original intent to align the effective dates applicable to nonpublic entities and public business entities that do not meet the definition of an SEC filer (for example, a broker-dealer), while providing additional time for nonpublic entities to implement the interim reporting requirements. Because the transition guidance in paragraph 326-10-65-1(c) requires that an entity make a cumulative-effect adjustment to opening retained earnings as of the beginning of the first reporting period in which the amendments are effective, stakeholders provided feedback that nonpublic entities would effectively be required to adopt CECL on January 1, 2021.

5. Because the Board had intended to provide nonpublic entities with additional time to implement interim reporting requirements of CECL, Update 2018-19 was issued to amend the effective date for nonpublic entities to annual and interim reporting periods beginning after December 15, 2021, align the annual and interim effective dates for nonpublic entities, and delay the effective date by one year beyond what was initially required by Update 2016-13.

6. On the basis of additional feedback from stakeholders and the Board's monitoring of the implementation of major Updates, in November 2019, the Board issued Accounting Standards Update No. 2019-10, *Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842): Effective Dates.* Update 2019-10 deferred the effective date of CECL for nonpublic entities by one year to annual and interim periods beginning after December 15, 2022.

7. In deciding to provide the deferral in Update 2019-10, the Board noted that implementation challenges often are magnified for private companies, smaller public companies, and not-for-profits, primarily because of the following factors (not all-inclusive):

   (a) Availability of resources (both internal and external)

   (b) Timing and source(s) of education

   (c) Knowledge or experience gained from implementation issues encountered by larger public companies

   (d) Comprehensive transition requirements

   (e) Understanding and applying guidance from post-issuance standard-setting activities

   (f) The development or acquisition of:

      (i) Sufficient information technology and expertise in creating new systems or effecting system changes

      (ii) Effective business solutions and internal controls

      (iii) Better data or estimation processes.

8. Several stakeholders submitted letters requesting that the Board defer the current effective date for entities that have not yet adopted CECL. Some letters also suggested that certain nonpublic entities should be excluded from being required to adopt CECL.