FASB issues ASU

New ASU affects receivable modification guidance and requires new disclosures

March 31, 2022

The FASB eliminates TDR recognition and measurement guidance for creditors and requires new disclosures.

Applicability

ASU 2022-02, Troubled Debt Restructurings and Vintage Disclosures

Applies to all entities after adopting Topic 326 (credit losses).

Fast facts, impacts, actions

ASU 2022-02 affects all creditors that have adopted Topic 326. It addresses two distinct areas.

Modifications of receivables to debtors experiencing financial difficulty under Topic 310 (receivables)	— Eliminates separate recognition and measurement guidance for troubled debt restructurings (TDRs), so creditors will apply the same guidance to all modifications when determining whether a modification results in a new receivable or a continuation of an existing receivable. — Requires expected credit losses measured under a discounted cash flow (DCF) method to be determined using an effective interest rate (EIR) based on the receivable's modified (not original) contractual terms for all modified receivables; a DCF (or reconcilable) method is no longer required for any modified receivables. — Enhances disclosures by creditors for modifications of receivables from debtors experiencing financial difficulty in the form of principal forgiveness, an interest rate reduction, an other-than-insignificant payment delay or a term extension.
Vintage disclosures under Topic 326	— Augments existing disclosures by requiring creditors that are public business entities to disclose current-period gross writeoffs by year of origination (i.e. the vintage year) for financing receivables and net investments in leases.

The ASU is applied prospectively to modifications and writeoffs beginning the first day of the fiscal year of adoption. However, a creditor may elect to adopt on a modified retrospective basis the effect on the allowance for credit losses related to the ASU's elimination of the TDR recognition and measurement guidance. See Effective dates and transition.

Action: Entities should start gathering information and developing processes to change how they measure the allowance for credit losses related to TDRs and to satisfy the new and enhanced disclosure requirements. Entities will need to evaluate a larger population of modifications to determine whether to account for them as new receivables or continuations of the existing receivables.

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee.

Modifications of receivables to debtors experiencing financial difficulty

Background

Under current US GAAP, a modification of a receivable is a TDR if the creditor grants a concession to a debtor experiencing financial difficulty. A modification that results in only a delay in payment that is insignificant is not considered a TDR.

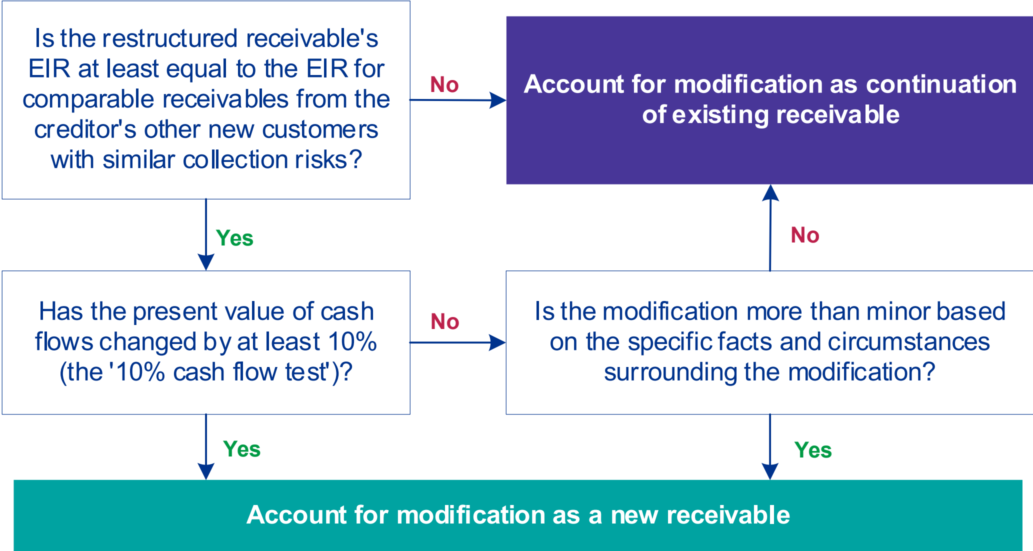
The accounting under current US GAAP for a receivable modification that is a TDR is summarized as follows.

- Unamortized deferred fees and costs from the original receivable are carried forward in the amortized cost basis of the modified receivable, with costs related to the modification expensed as incurred.
- The EIR used when a DCF (or reconcilable) method is used to measure expected credit losses is based on the original contractual rate; a DCF (or reconcilable) method is **required** to measure the expected credit losses for certain TDRs.

In connection with its post-implementation review of Topic 326, the FASB was informed by stakeholders that designation of a receivable modification as a TDR and the related accounting and disclosure are unnecessarily complex and no longer provide decision-useful information under a lifetime expected credit loss model. In response, the FASB decided to eliminate the TDR recognition and measurement guidance and enhance disclosures for modifications of receivables from debtors experiencing financial difficulty.

Elimination of TDR recognition and measurement guidance

The ASU eliminates the recognition and measurement guidance for TDRs by creditors. Instead, creditors will evaluate how to account for modifications that had been subject to the TDR guidance using the following decision tree.



Observation: In most cases, receivable modifications that were historically considered TDRs will be treated as continuations of an existing receivable because they will not have a market EIR.

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee.

The following table summarizes the accounting for all receivable modifications after adopting the ASU.

Continuation of existing receivable (Subtopic 310-20)	— Unamortized deferred fees and costs are carried forward in the amortized cost basis of the modified receivable, along with any new fees received and direct costs associated with the restructuring. — A 'post-modification derived EIR' (i.e. an EIR based on the modified terms) is used when a DCF method is used to measure expected credit losses; a DCF method is **not required**.
New receivable (Subtopic 310-20)	— Unamortized deferred fees and costs associated with the original receivable and any prepayment penalties are recognized in interest income. — A new receivable is recognized. — A post-modification EIR is used when a DCF method is used to measure expected credit losses; a DCF method is **not required**.

Observation: Topic 326 currently provides specific guidance on measuring credit losses for TDRs. Because the effects of certain concessions can be captured only through a DCF method, a DCF (or reconcilable) method is required for measuring expected credit losses for some TDRs – e.g. interest rate concessions or more than insignificant delays in payment (i.e. term extensions or forbearances). After adopting the ASU, an entity will no longer be required to use a DCF method and will use an EIR based on the post-modified contractual rate. These changes will generally result in smaller allowances for credit losses for modifications that previously would have applied the TDR guidance.

Enhanced disclosures for modifications of receivables from debtors experiencing financial difficulty

The ASU also enhances disclosure requirements by creditors for modifications of receivables from debtors experiencing financial difficulty in the form of principal forgiveness, an interest rate reduction, an other-than-insignificant payment delay or a term extension. A covenant waiver or modification of a contingent acceleration clause is not considered a term extension. The disclosure requirements apply regardless of whether the creditor determines that the modification represents a continuation of the existing receivable or a new receivable.

Observation: The ASU's guidance for determining whether a debtor is 'experiencing financial difficulty' and whether a modification results only in a 'delay in payment that is insignificant' is largely the same as existing guidance used to determine whether a modification is a TDR. However, under the ASU, an entity only considers the cumulative effect of restructurings made within the 12-month period before the current restructuring when determining whether a delay in payment resulting from the current restructuring is insignificant.

The objective of the disclosures is to provide financial statement users with information about the type and magnitude of modifications of receivables from debtors experiencing financial difficulty, the financial effect of those modifications, and the degree of success of the modifications in mitigating potential credit losses. The required disclosures include:

— the types of modifications used by the creditor;

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee.

- the financial effect of modifications, by type of modification, including information about the changes to the contractual terms as a result of the modifications;
- receivable performance in the 12 months after its modification;
- qualitative information about how the modifications and the debtors' subsequent performance are factored into determining the allowance for credit losses; and
- the amount of commitments, if any, to lend additional funds to debtors experiencing financial difficulty that entered into a modification.

Observation: The enhanced disclosures will be broader in scope than the disclosures for modifications of receivables previously considered to be TDRs.

The ASU provides an example to illustrate how an entity might meet the enhanced disclosure requirements based on specific facts and circumstances.

Vintage disclosures – gross writeoffs

Financial statement users informed the FASB that disclosure of gross writeoffs by year of origination provides particularly important information that allows them to better understand changes in the credit quality of a creditor's receivable portfolio and underwriting performance.

As a result of this feedback, the ASU requires a public business entity to disclose current-period gross writeoffs by year of origination for financing receivables and net investments in leases in the scope of Subtopic 326-20.

Observation: The FASB chose not to require disclosure of gross recoveries. The ASU amends the illustrative disclosure of credit quality indicators in Subtopic 326-20 by removing the gross recovery information.

Effective dates and transition

	Entities that have adopted Topic 326	Other entities
Annual and interim periods – Fiscal years beginning after	December 15, 2022	December 15, 2022; consistent with when the entity first applies Topic 326
Early adoption permitted?	Yes; early adoption is permitted for an entity that has adopted Topic 326 in any interim period as of the beginning of the fiscal year that includes the interim period. An entity may elect to early adopt the amendments related to receivable modifications separately from the amendments related to vintage disclosures.	

Transition provisions

The amendments in the ASU are applied prospectively to modifications and writeoffs after the first day of the fiscal year of adoption. However, related to the elimination of recognition and measurement of TDRs by creditors, an entity can elect to apply the ASU on a modified retrospective basis to recognize any change in the allowance for credit losses that had been recognized for receivables previously modified (or

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee.

reasonably expected to be modified) in a TDR. This election would result in a cumulative-effect adjustment to retained earnings as of the beginning of the fiscal year of adoption.

Action: An entity that elects to early adopt in an interim period (other than the initial interim period of the fiscal year) will need to determine the impact of applying all aspects of the guidance during the previous interim periods within the fiscal year. For example, an entity would need to reevaluate whether receivables modified in TDRs in previous interim periods within the fiscal year would be accounted for as new receivables rather than continuations of the existing receivables.

Contributing authors

Mark Northan, Lisa Blackburn, Tyler McKamy

KPMG Financial Reporting View

kpmg.com/us/frv

This newsletter is part of our Defining Issues® collection of newsletters and articles with insights and news about financial reporting and regulatory developments.

Sign up here to receive news and insights delivered to your mailbox.

kpmg.com/socialmedia

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization.

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.