FASB EXPOSURE DRAFT

Proposed Accounting Standards Update

Issued: January 10, 2017
Comments Due: May 5, 2017

Debt (Topic 470)

Simplifying the Classification of Debt in a Classified Balance Sheet (Current versus Noncurrent)

The Board issued this Exposure Draft to solicit public comment on proposed changes to Topic 470 of the *FASB Accounting Standards Codification*®. Individuals can submit comments in one of three ways: using the electronic feedback form on the FASB website, emailing comments to director@fasb.org, or sending a letter to "Technical Director, File Reference No. 2017-200, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116."

Financial Accounting Standards Board

Notice to Recipients of This Exposure Draft of a Proposed Accounting Standards Update

The Board invites comments on all matters in this Exposure Draft until May 5, 2017. Interested parties may submit comments in one of three ways:

- Using the electronic feedback form available on the FASB website at Exposure Documents Open for Comment
- Emailing comments to director@fasb.org, File Reference No. 2017-200
- Sending a letter to "Technical Director, File Reference No. 2017-200, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116."

All comments received are part of the FASB's public file and are available at www.fasb.org.

The *FASB Accounting Standards Codification*® is the source of authoritative generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. An Accounting Standards Update is not authoritative; rather, it is a document that communicates how the Accounting Standards Codification is being amended. It also provides other information to help a user of GAAP understand how and why GAAP is changing and when the changes will be effective. A copy of this Exposure Draft is available at www.fasb.org.

FASB FINANCIAL ACCOUNTING STANDARDS BOARD

Proposed Accounting Standards Update

Debt (Topic 470)

Simplifying the Classification of Debt in a Classified Balance Sheet (Current versus Noncurrent)

January 10, 2017

Comment Deadline: May 5, 2017

CONTENTS

Summary and Questions for Respondents

Why Is the FASB Issuing This Proposed Accounting Standards Update (Update)?

The Board is issuing this proposed Update as part of its Simplification Initiative. The objective of the Simplification Initiative is to identify, evaluate, and improve areas of generally accepted accounting principles (GAAP) for which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to users of the financial statements.

Stakeholders have told the Board that the guidance on determining whether debt should be classified as current or noncurrent in a classified balance sheet is overly complex. Topic 470, Debt, includes guidance on various narrow-scope, fact-specific debt transactions. The amendments in this proposed Update would replace the current, fact-specific guidance with an overarching, cohesive principle. The Board expects that the proposed amendments would reduce the cost and complexity for preparers and auditors when determining whether debt should be classified as current or noncurrent in the balance sheet while providing more consistent and transparent information to financial statement users.

Who Would Be Affected by the Amendments in This Proposed Update?

The balance sheet of most entities shows separate classification of current assets and current liabilities (commonly referred to as a classified balance sheet) permitting ready determination of working capital. The amendments in this proposed Update relate to separate classifications of current debt and noncurrent debt within a classified balance sheet. An entity that does not present a classified balance sheet would be unaffected by the proposed amendments.

The amendments in this proposed Update would apply to all entities that enter into a debt arrangement. A debt arrangement provides a lender with a contractual right to receive consideration and a borrower with a contractual obligation to pay consideration on demand or on fixed or determinable dates. The proposed amendments also would apply to convertible debt instruments and liability-classified mandatorily redeemable financial instruments.

What Are the Main Provisions and Why Would They Be an Improvement?

The amendments in this proposed Update introduce a principle for determining whether a debt arrangement, or other instrument within the scope of this proposed Update, should be classified as a noncurrent liability as of the balance sheet date. That principle is that an entity should classify an instrument as noncurrent if either of the following criteria is met as of the balance sheet date:

1. The liability is contractually due to be settled more than one year (or operating cycle, if longer) after the balance sheet date.
2. The entity has a contractual right to defer settlement of the liability for at least one year (or operating cycle, if longer) after the balance sheet date.

The amendments in this proposed Update would continue to require an entity to classify a debt arrangement as a noncurrent liability when there has been a debt covenant violation, if the entity receives a waiver of that violation that meets certain conditions before the financial statements are issued (or are available to be issued). That classification is an exception to the principle above, but is similar to current GAAP. The exception would apply to all waivers except for those that result in a *troubled debt restructuring* (as defined in the Master Glossary of the Codification) or those that are accounted for as a debt extinguishment in Subtopic 470-50, Debt—Modifications and Extinguishments. The Board also decided to retain and clarify the probability assessment related to subsequent covenant violations. The proposed amendments also would require an entity to separately present in the balance sheet liabilities that are classified as noncurrent as a result of this exception.

The amendments in this proposed Update could shift classification of certain debt arrangements between noncurrent liabilities and current liabilities as compared with current guidance. The existing classification guidance would be superseded by a principle that may differ from existing rules that the proposed amendments would eliminate.

One of the most significant changes to the classification would be, for example, short-term debt that is refinanced on a long-term basis after the balance sheet date. Current guidance requires short-term debt (at the balance sheet date) that is refinanced on a long-term basis (after the balance sheet date but before the financial statements are issued or are available to be issued) to be classified as a noncurrent liability. The amendments in this proposed Update would prohibit an entity from considering a subsequent refinancing when determining the classification of debt as of the balance sheet date. A subsequent refinancing provides evidence about conditions that did not exist at the date of the balance sheet but arose after that date (that is, a nonrecognized subsequent event). Similarly, a subsequent refinancing of short-term debt with the issuance of equity securities would no longer affect the classification of debt as of the balance sheet date under the proposed amendments. Therefore, those debt arrangements would be classified as current liabilities.

Another example of a change in classification results from debt that contains subjective acceleration clauses or material adverse change clauses. Current GAAP requires entities to consider the likelihood of acceleration of the due date when determining noncurrent or current classification. The amendments in this proposed Update would remove that probability assessment. Instead, the subjective acceleration clause would impact classification of debt only when it is triggered.

When Would the Amendments Be Effective?

In the first set of interim and annual financial statements following the effective date, an entity would apply the amendments in this proposed Update on a prospective basis to debt that exists at that date and after that date. Early adoption of the proposed amendments would be permitted. The Board will determine the effective date after it considers stakeholder feedback on the proposed amendments.

Questions for Respondents

The Board invites individuals and organizations to comment on all matters in this proposed Update, particularly on the issues and questions below. Comments are requested from those who agree with the proposed guidance as well as from those who do not agree. Comments are most helpful if they identify and clearly explain the issue or question to which they relate. Those who disagree with the proposed guidance are asked to describe their suggested alternatives, supported by specific reasoning.

Question 1: Paragraph 470-10-45-22 includes a principle for classifying debt as a noncurrent liability in a classified balance sheet. Would the proposed principle simplify the classification guidance in GAAP without diminishing the usefulness of the information provided in the financial statements? Is the proposed principle clear? Why or why not? Please explain and suggest alternatives.

Question 2: The scope of the amendments in this proposed Update includes debt arrangements as well as (a) liability-classified mandatorily redeemable financial instruments within the scope of Topic 480, Distinguishing Liabilities from Equity, and (b) debt with conversion and other options that are within the scope of Subtopic 470-20, Debt—Debt with Conversion and Other Options. Is the scope of the proposed amendments clear? Why or why not? Are there any other instruments that should be included within the scope of the proposed amendments? If so, please explain.

Question 3: Paragraph 470-10-45-23 includes an exception to the classification principle for waivers of debt covenant violations received after the reporting date but before the financial statements are issued (or are available to be issued). Will including this exception reduce the cost of the proposed amendments? Why or why not? Please explain and suggest alternatives.

Question 4: Paragraph 470-10-45-24 would require separate presentation in a classified balance sheet for debt that is classified as a noncurrent liability because of a waiver of a debt covenant violation received after the reporting date but before the financial statements are issued (or are available to be issued). Does separate presentation of this amount provide decision-useful information for those using the financial statements? Why or why not? Please explain and suggest alternatives.

Question 5: The proposed amendments would require an entity to classify as a current liability a debt arrangement that is short-term debt (at the balance sheet date) but that is subsequently refinanced as long-term debt (after the balance sheet date but before the financial statements are issued). That would result in more current liabilities and less noncurrent liabilities, as compared with current GAAP. Do you agree that these refinancings are nonrecognized subsequent events? If not, please explain why and suggest alternatives.

Question 6: Paragraph 470-10-50-6 provides new disclosure requirements. Do the proposed disclosure requirements provide decision-useful information? If not, please explain why and suggest alternatives.

Question 7: How much time would be necessary to adopt the proposed amendments? Would the amount of time needed to apply the proposed amendments by entities other than public business entities be different from the amount of time needed by public business entities? Do you agree that early adoption should be permitted?

Amendments to the *FASB Accounting Standards Codification*®

Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–14. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is <u>underlined</u>, and deleted text is ~~struck out~~.

Amendments to Master Glossary

2. Add the new Master Glossary term *Debt Arrangement*, with a link to transition paragraph 470-10-65-1, as follows:

<u>**Debt Arrangement**</u>

<u>An arrangement that provides a lender with a contractual right to receive consideration and a borrower with a contractual obligation to pay consideration on demand or on fixed or determinable dates.</u>

3. Supersede the following Master Glossary terms, with a link to transition paragraph 470-10-65-1, as follows:

~~**Lock-Box Arrangement**~~

~~An arrangement with a lender whereby the borrower's customers are required to remit payments directly to the lender and amounts received are applied to reduce the debt outstanding. A lock-box arrangement refers to any situation in which the borrower does not have the ability to avoid using working capital to repay the amounts outstanding. That is, the contractual provisions of a loan arrangement require that, in the ordinary course of business and without another event occurring, the cash receipts of a debtor are used to repay the existing obligation.~~

~~**Springing Lock-Box Arrangement**~~

~~Some borrowings outstanding under a revolving credit agreement include both a subjective acceleration clause and a requirement to maintain a springing lock-box arrangement, whereby remittances from the borrower's customers are forwarded~~

~~to the debtor's general bank account and do not reduce the debt outstanding until and unless the lender exercises the subjective acceleration clause.~~

Amendments to Subtopic 470-10

4. Amend paragraph 470-10-05-5 and add paragraphs 470-10-05-6 and 470-10-15-3 through 15-4, with a link to transition paragraph 470-10-65-1, as follows:

Debt—Overall

Overview and Background

470-10-05-5 The Overall Subtopic addresses classification ~~determination~~ for a **debt arrangement,** a liability-classified **mandatorily redeemable financial instrument** within the scope of Subtopic 480-10 on distinguishing liabilities from equity, and debt with conversion and other options that are within the scope of Subtopic 470-20.~~specific obligations, such as the following:~~

a. Subparagraph superseded by Accounting Standards Update No. 201X-XX.~~Short-term obligations expected to be refinanced on a long-term basis.~~
b. Subparagraph superseded by Accounting Standards Update No. 201X-XX.~~Due-on-demand loan arrangements.~~
c. Subparagraph superseded by Accounting Standards Update No. 201X-XX.~~Callable debt~~
d. Subparagraph superseded by Accounting Standards Update No. 201X-XX.~~Sales of future revenue~~
e. Subparagraph superseded by Accounting Standards Update No. 201X-XX.~~Increasing-rate debt~~
f. Subparagraph superseded by Accounting Standards Update No. 201X-XX.~~Debt that includes covenants~~
g. Subparagraph superseded by Accounting Standards Update No. 201X-XX.~~Revolving credit agreements subject to lock-box arrangements and subjective acceleration clauses~~
h. Subparagraph superseded by Accounting Standards Update No. 201X-XX.~~Indexed debt.~~

470-10-05-6 ~~Paragraph not used.~~This Subtopic also includes measurement guidance for increasing rate debt, sales of future revenue, and indexed debt.

Scope and Scope Exceptions

> Entities

470-10-15-1 The guidance in this Subtopic applies to all entities.

> Transactions

470-10-15-2 The guidance in this Subtopic that relates to separate classification of current assets and current liabilities (that is, a classified balance sheet) applies only when an entity is preparing a classified balance sheet for financial accounting and reporting purposes.

470-10-15-3 The Overall Subtopic addresses classification of current and noncurrent liabilities that arise from a **debt arrangement**. Examples of debt arrangements include the following:

a. Term debt
b. Due-on-demand loan agreements
c. Callable debt agreements
d. Increasing-rate debt
e. Debt that includes covenants
f. Revolving credit arrangements
g. Debt with a **subjective acceleration clause**
h. Indexed debt
i. Proceeds from sales of future revenue that are classified as debt.

470-10-15-4 The classification guidance for current and noncurrent liabilities in this Subtopic also applies to the following:

a. A liability-classified **mandatorily redeemable financial instrument** within the scope of Subtopic 480-10 on distinguishing liabilities from equity
b. Debt with conversion or other options that is within the scope of Subtopic 470-20.

5. Add paragraph 470-10-35-2A, with a link to transition paragraph 470-10-65-1, as follows:

Subsequent Measurement

> Increasing Rate Debt

470-10-35-1 A debt instrument may have a maturity date that can be extended at the option of the borrower at each maturity date until final maturity. In such cases, the interest rate on the note increases a specified amount each time the note is renewed. For guidance on accounting for interest, see Subtopic 835-30.

470-10-35-2 The borrower's periodic interest cost shall be determined using the interest method based on the estimated outstanding term of the debt. In estimating the term of the debt, the borrower shall consider its plans, ability, and intent to service the debt. Debt issue costs shall be amortized over the same period used in the interest cost determination. The term-extending provisions of the debt instrument should be analyzed to determine whether those provisions constitute an embedded derivative that warrants separate accounting as a derivative under Subtopic 815-10.

470-10-35-2A If the debt is paid at par before its estimated maturity, any excess interest accrued shall be an adjustment of interest expense. **[Content moved from paragraph 470-10-45-8]**

6. Supersede paragraphs 470-10-45-1 through 45-21 and their related headings and add paragraphs 470-10-45-22 through 45-24 and their related headings, with a link to transition paragraph 470-10-65-1, as follows:

Other Presentation Matters

~~> Classification of Debt That Includes Covenants~~

470-10-45-1 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~Some long-term loans require compliance with certain covenants that must be met on a quarterly or semiannual basis. If a covenant violation occurs that would otherwise give the lender the right to call the debt, a lender may waive its call right arising from the current violation for a period greater than one year while retaining future covenant requirements. Unless facts and circumstances indicate otherwise, the borrower shall classify the obligation as noncurrent, unless both of the following conditions exist:~~

~~a. A covenant violation that gives the lender the right to call the debt has occurred at the balance sheet date or would have occurred absent a loan modification.~~
~~b. It is probable that the borrower will not be able to cure the default (comply with the covenant) at measurement dates that are within the next 12 months.~~

~~See Example 1 (paragraph 470-10-55-2) for an illustration of this classification guidance.~~ **[Content amended and moved to paragraph 470-10-45-23]**

~~**> Subjective Acceleration Clauses and Debt Classification**~~

470-10-45-2 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~In some situations, the circumstances (for example, recurring losses or liquidity problems) would indicate that long-term debt subject to a **subjective acceleration clause** should be classified as a current liability. Other situations would indicate only disclosure of the existence of such clauses. Neither reclassification nor disclosure would be required if the likelihood of the acceleration of the due date were remote, such as if the lender historically has not accelerated due dates of loans containing similar clauses and the financial condition of the borrower is strong and its prospects are bright.~~

~~**> Classification of Revolving Credit Agreements Subject to Lock-Box Arrangements and Subjective Acceleration Clauses**~~

470-10-45-3 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~This guidance does not apply to lock-box arrangements that are maintained at the discretion of the borrower.~~

470-10-45-4 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~Borrowings outstanding under certain revolving credit agreements are considered long-term debt because the borrowings are due at the end of a specified period (for example, 3 years) rather than when short-term notes roll over (for example, every 90 days). Borrowings may be collateralized, but the only note is the overall note signed at the agreement's inception. Some agreements require that the borrower maintain a **lock-box arrangement**. If borrowings outstanding under the agreement are considered **long-term obligations**, the effect of a subjective acceleration clause on balance sheet classification is determined based on the criteria in paragraph 470-10-45-2. If borrowings outstanding are considered short-term obligations, and the borrower intends to refinance the obligation on a long-term basis, paragraph 470-10-45-13 applies and the debt shall be classified as a current liability because of the existence of the subjective acceleration clause.~~

470-10-45-5 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~Borrowings outstanding under a revolving credit agreement that includes both a subjective acceleration clause and a requirement to maintain a lock-box arrangement shall be considered short-term obligations. Accordingly, because of the subjective acceleration clause, the debt shall be classified as a current liability unless the conditions in paragraph 470-10-45-14 are met based on an agreement, other than the revolving credit agreement, to refinance the obligation after the balance sheet date on a long-term basis.~~

470-10-45-5A Paragraph superseded by Accounting Standards Update No. 201X-XX.~~The term *lock-box arrangement* as used in this guidance refers to any situation in which the borrower does not have the ability to avoid using working capital to~~

~~repay the amounts outstanding. That is, if the contractual provisions of a loan arrangement require that, in the ordinary course of business and without another event occurring, the cash receipts of a debtor be used to repay the existing obligation, the credit agreement shall be considered a short-term obligation.~~

470-10-45-6 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~Borrowings outstanding under a revolving credit agreement that includes both a subjective acceleration clause and a requirement to maintain a **springing lock-box arrangement** shall be considered long-term obligations since the remittances do not automatically reduce the debt outstanding without another event occurring. The effect of the agreement's subjective acceleration clause shall be determined based on the provisions of paragraph 470-10-45-2.~~

~~> Classification of Increasing-Rate Debt~~

470-10-45-7 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~Classification of increasing-rate debt as current or noncurrent would reflect the borrower's anticipated source of repayment that is, current assets or a new short-term debt borrowing versus a long-term refinancing agreement that meets the requirements of this Subtopic and need not be consistent with the time frame used to determine periodic interest cost.~~

470-10-45-8 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~If the debt is paid at par before its estimated maturity, any excess interest accrued shall be an adjustment of interest expense.~~ **[Content moved to paragraph 470-10-35-2A]**

~~> Due on Demand Loan Arrangements~~

470-10-45-9 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~Loan agreements may specify the debtor's repayment terms but also enable the creditor, at his discretion, to demand payment at any time. Those loan arrangements may have wording such as either of the following:~~

- ~~a. "The term note shall mature in monthly installments as set forth therein or on demand, whichever is earlier."~~
- ~~b. "Principal and interest shall be due on demand, or if no demand is made, in quarterly installments beginning on…."~~

470-10-45-10 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~The current liability classification shall include obligations that, by their terms, are due on demand or will be due on demand within one year (or **operating cycle**, if longer) from the balance sheet date, even though liquidation may not be~~

~~expected within that period. The demand provision is not a subjective acceleration clause as discussed in paragraph 470-10-45-2.~~

~~**> Callable Debt**~~

470-10-45-11 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~Current liabilities shall include long-term obligations that are or will be callable by the creditor either because the debtor's **violation of a provision** of the debt agreement at the balance sheet date makes the **obligation callable** or because the violation, if not cured within a specified grace period, will make the obligation callable. Accordingly, such callable obligations shall be classified as current liabilities unless either of the following conditions is met:~~

- ~~a. The creditor has waived or subsequently lost (for example, the debtor has cured the violation after the balance sheet date and the obligation is not callable at the time the financial statements are issued or are available to be issued [as discussed in Section 855-10-25]) the right to demand repayment for more than one year (or operating cycle, if longer) from the balance sheet date. If the obligation is callable because of violations of certain provisions of the debt agreement, the creditor needs to waive its right with regard only to those violations.~~
- ~~b. For long-term obligations containing a grace period within which the debtor may cure the violation, it is **probable** that the violation will be cured within that period, thus preventing the obligation from becoming callable.~~

470-10-45-12 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~Drawing a distinction between significant violations of critical conditions and technical violations is not practicable. A violation that a debtor considers to be technical may be considered critical by the creditor. Furthermore, a creditor may choose to use a technical violation as a means to withdraw from its lending relationship with the debtor. If the violation is considered insignificant by the creditor, then the debtor should be able to obtain a waiver as discussed in the preceding paragraph.~~

~~**> Short-Term Obligations Expected to Be Refinanced**~~

470-10-45-12A <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~Some short-term obligations are expected to be refinanced on a long-term basis and, therefore, are not expected to require the use of working capital during the ensuing fiscal year. Examples include commercial paper, construction loans, and the currently maturing portion of long-term debt.~~

470-10-45-12B Paragraph superseded by Accounting Standards Update No. 201X-XX.~~Refinancing a short-term obligation on a long-term basis means either replacing it with a long-term obligation or with equity securities or renewing, extending, or replacing it with short-term obligations for an uninterrupted period extending beyond one year (or the operating cycle, if applicable) from the date of an entity's balance sheet.~~

470-10-45-13 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~Short-term obligations arising from transactions in the normal course of business that are due in customary terms shall be classified as current liabilities. A short-term obligation shall be excluded from current liabilities only if the conditions in the following paragraph are met. Funds obtained on a long-term basis before the balance sheet date would be excluded from current assets if the obligation to be liquidated is excluded from current liabilities~~.

~~> Intent and Ability to Refinance on a Long-Term Basis~~

470-10-45-14 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~A short-term obligation shall be excluded from current liabilities if the entity intends to refinance the obligation on a long-term basis (see paragraph 470-10-45-12B) and the intent to refinance the short-term obligation on a long-term basis is supported by an ability to consummate the refinancing demonstrated in either of the following ways:~~

- ~~a. Post-balance-sheet-date issuance of a long-term obligation or equity securities. After the date of an entity's balance sheet but before that balance sheet is issued or is available to be issued (as discussed in Section 855-10-25), a long-term obligation or equity securities have been issued for the purpose of refinancing the short-term obligation on a long-term basis. If equity securities have been issued, the short-term obligation, although excluded from current liabilities, shall not be included in owners' equity.~~
- ~~b. Financing agreement. Before the balance sheet is issued or is available to be issued (as discussed in Section 855-10-25), the entity has entered into a financing agreement that clearly permits the entity to refinance the short-term obligation on a long-term basis on terms that are readily determinable, and all of the following conditions are met:~~
  - ~~1. The agreement does not expire within one year (or operating cycle) from the date of the entity's balance sheet and during that period the agreement is not cancelable by the lender or the prospective lender or investor (and obligations incurred under the agreement are not callable during that period) except for violation of a provision with which compliance is objectively determinable or measurable. For~~

~~purposes of this Subtopic, violation of a provision means failure to meet a condition set forth in the agreement or breach or violation of a provision such as a restrictive covenant, representation, or warranty, whether or not a grace period is allowed or the lender is required to give notice. Financing agreements cancelable for violation of a provision that can be evaluated differently by the parties to the agreement (such as a material adverse change or failure to maintain satisfactory operations) do not comply with this condition.~~

~~2. No violation of any provision in the financing agreement exists at the balance sheet date and no available information indicates that a violation has occurred thereafter but before the balance sheet is issued or is available to be issued (as discussed in Section 855-10-25), or, if one exists at the balance sheet date or has occurred thereafter, a waiver has been obtained.~~

~~3. The lender or the prospective lender or investor with which the entity has entered into the financing agreement is expected to be financially capable of honoring the agreement.~~

470-10-45-15 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~Repayment of a short-term obligation before funds are obtained through a long-term refinancing requires the use of current assets. Therefore, if a short-term obligation is repaid after the balance sheet date and subsequently a long-term obligation or equity securities are issued whose proceeds are used to replenish current assets before the balance sheet is issued or is available to be issued (as discussed in Section 855-10-25), the short-term obligation shall not be excluded from current liabilities at the balance sheet date. See Example 5 (paragraph 470-10-55-33) for an illustration of this guidance.~~

470-10-45-16 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~If an entity's ability to consummate an intended refinancing of a short-term obligation on a long-term basis is demonstrated by post-balance-sheet-date issuance of a long-term obligation or equity securities (see paragraph 470-10-45-14(a)), the amount of the short-term obligation to be excluded from current liabilities shall not exceed the proceeds of the new long-term obligation or the equity securities issued.~~

470-10-45-17 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~If ability to refinance is demonstrated by the existence of a financing agreement (see paragraph 470-10-45-14(b)), the amount of the short-term obligation to be excluded from current liabilities shall be reduced to the amount available for refinancing under the agreement if the amount available is less than the amount of the short-term obligation.~~

470-10-45-18 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~The amount to be excluded shall be reduced further if information (such as~~

~~restrictions in other agreements or restrictions as to transferability of funds) indicates that funds obtainable under the agreement will not be available to liquidate the short-term obligation.~~

470-10-45-19 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~Further, if amounts that could be obtained under the financing agreement fluctuate (for example, in relation to the entity's needs, in proportion to the value of collateral, or in accordance with other terms of the agreement), the amount to be excluded from current liabilities shall be limited to a reasonable estimate of the minimum amount expected to be available at any date from the scheduled maturity of the short-term obligation to the end of the fiscal year (or operating cycle). If no reasonable estimate can be made, the entire outstanding short-term obligation shall be included in current liabilities.~~

470-10-45-20 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~The entity may intend to seek an alternative source of financing rather than to exercise its rights under the existing agreement when the short-term obligation becomes due. The entity must intend to exercise its rights under the existing agreement, however, if that other source does not become available. The intent to exercise may not be present if the terms of the agreement contain conditions or permit the prospective lender or investor to establish conditions, such as interest rates or collateral requirements, that are unreasonable to the entity.~~

~~> Transactions after the Balance Sheet Date~~

470-10-45-21 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~Replacement of a short-term obligation with another short-term obligation after the date of the balance sheet but before the balance sheet is issued or is available to be issued (as discussed in Section 855-10-25) is not, by itself, sufficient to demonstrate an entity's ability to refinance the short-term obligation on a long-term basis. If, for example, the replacement is made under the terms of a revolving credit agreement that provides for renewal or extension of the short-term obligation for an uninterrupted period extending beyond one year (or operating cycle) from the date of the balance sheet, the revolving credit agreement must meet the conditions in paragraph 470-10-45-14(b) to justify excluding the short-term obligation from current liabilities. Similarly, if the replacement is a rollover of commercial paper accompanied by a standby credit agreement, the standby agreement must meet the conditions in that paragraph to justify excluding the short-term obligation from current liabilities.~~

> Classification of Debt

470-10-45-22 Debt arrangements and other instruments within the scope of this Subtopic (see paragraphs 470-10-15-3 through 15-4) shall be classified as noncurrent liabilities in a classified balance sheet if either of the following criteria is met as of the balance sheet date:

a. The liability is contractually due to be settled more than one year (or **operating cycle**, if longer) after the balance sheet date.
b. The entity has a contractual right to defer settlement of the liability for at least one year (or operating cycle, if longer) after the balance sheet date.

An exception to this principle is described in paragraph 470-10-45-23.

> Classification of Debt ~~That Includes Covenants~~Subject to a Covenant Violation

470-10-45-23 Some long-term loans require compliance with certain covenants that must be met on a periodic or ongoing~~quarterly or semiannual~~ basis. ~~If a covenant violation occurs that would otherwise give the lender the right to call the debt, a~~A lender may waive its ~~call~~ right to demand payment arising from ~~the~~a current covenant violation for a period greater than one year (or **operating cycle**, if longer) after the balance sheet date while retaining other future covenant requirements. ~~Unless facts and circumstances indicate otherwise, the~~The borrower shall classify the obligation as a noncurrent liability in a classified balance sheet, ~~unless both~~if all of the following conditions exist:

a. ~~A covenant violation that gives the lender the right to call the debt has occurred at the balance sheet date or would have occurred absent a loan modification.~~One of the criteria in paragraph 470-10-45-22 would have been met absent the covenant violation.
b. ~~It is probable that the borrower will not be able to cure the default (comply with the covenant) at measurement dates that are within the next 12 months.~~A waiver of the violation has been obtained by the borrower before the date that the **financial statements are issued** (or the date that the **financial statements are available to be issued**). The waiver is for a period greater than one year (or operating cycle, if longer) from the balance sheet date.
c. At the time the waiver is granted, the waiver for the debt arrangement does not result in a modification that is either:
   1. An extinguishment of debt accounted for in accordance with guidance in Subtopic 470-50
   2. A **troubled debt restructuring** accounted for in accordance with Subtopic 470-60.
d. It is not probable that any other covenants in the debt arrangement (for example, other covenants not included in the waiver) will be violated within 12 months (or operating cycle, if longer) from the balance sheet date.

See ~~Example 1 (paragraph 470-10-55-2)~~paragraphs 470-10-55-2 through 55-3F for ~~an illustration~~illustrations of this ~~classification~~ guidance. **[Content amended as shown and moved from paragraph 470-10-45-1]**

470-10-45-24 An entity shall separately present, in a classified balance sheet, the amount of debt that is classified as a noncurrent liability because of waivers obtained after the balance sheet date.

7. Supersede paragraphs 470-10-50-3 through 50-4 and their related headings and add paragraph 470-10-50-6 and its related heading, with a link to transition paragraph 470-10-65-1, as follows:

Disclosure

~~> Subjective Acceleration Clauses~~

470-10-50-3 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~As indicated in paragraph 470-10-45-2, in some situations long-term debt subject to a **subjective acceleration clause** shall be reclassified. That paragraph explains that other situations would indicate only disclosure of the existence of such clauses. That paragraph states further that neither reclassification nor disclosure is required if the likelihood of the acceleration of the due date is remote, such as when the lender historically has not accelerated due dates of loans containing similar clauses and the financial condition of the borrower is strong and its prospects are bright.~~

~~> Short-Term Obligations Expected to Be Refinanced~~

470-10-50-4 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~If a short-term obligation is excluded from current liabilities pursuant to the provisions of this Subtopic, the notes to financial statements shall include a general description of the financing agreement and the terms of any new obligation incurred or expected to be incurred or equity securities issued or expected to be issued as a result of a refinancing.~~

> Defaults

470-10-50-6 Events of default include violations of a loan covenant and triggers of a **subjective acceleration clause** (for example, when the borrower is notified by the lender of noncompliance). An entity shall disclose the following information about any events of default:

a. An explanation of the deficiency

b. <u>The amount of obligations subject to the default</u>
c. <u>The terms of a waiver (including period of the waiver, if applicable)</u>
d. <u>A description of the course of action that the entity has taken, or that it proposes to take, to remedy the deficiency.</u>

8. Supersede paragraphs 470-10-55-1, 470-10-55-4 through 55-6, 470-10-55-13 through 55-36 and their related headings, amend paragraphs 470-10-55-2 through 55-3 and 470-10-55-7 through 55-9, and add paragraphs 470-10-55-3A through 55-3F and their related headings and 470-10-55-37 through 55-45 and their related headings, with a link to transition paragraph 470-10-65-1, as follows:

Implementation Guidance and Illustrations

~~> Implementation Guidance~~

~~> > Subjective Acceleration Clauses and Debt Classification~~

470-10-55-1 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~Under paragraph 470-10-45-2, the lender has already loaned money on a long-term basis. To continue long-term classification requires a judgment about the likelihood of acceleration of the due date. Paragraphs 470-10-45-13 through 45-20 cover circumstances in which the obligation is by its terms short-term. For such an obligation to be excluded from current liabilities, the lender must advance new funds or refinance the short-term obligation on a long-term basis based on conditions existing on the date of the new loan or refinancing. Therefore, to classify an obligation as long-term, paragraphs 470-10-45-13 through 45-20 require a higher standard for a financing agreement that permits an entity to refinance a short-term obligation on a long-term basis than paragraph 470-10-50-2 requires for an existing long-term loan for which early repayment might be requested.~~

> Illustrations

> > Example 1: Classification of Long-Term Debt that Includes Covenants

470-10-55-2 ~~This Example illustrates~~<u>The following Cases illustrate </u>the guidance in ~~paragraph 470-10-45-1~~<u>paragraphs 470-10-45-22 through 45-24 </u>for the classification of ~~long-term~~ debt when a debt covenant violation is waived by a lender for a period greater than a year.

<u>> > > Case A: Debt Is Classified as Noncurrent</u>

470-10-55-3 A borrower has a long-term loan that requires compliance with certain covenants, such as maintenance of a minimum current ratio, minimum debt-to-equity ratio, or minimum level of shareholders' equity. The borrower must meet the covenants on a periodic or ongoing~~quarterly or semiannual~~ basis. If the borrower does not comply with any one of these covenants, the lender can demand repayment of the loan. At one of the compliance dates, December 31, 20X1, the borrower violates a covenant. The borrower performs the calculation of the December 31, 20X1 covenant compliance in January 20X2. That violation gives the lender the right to ~~call~~demand payment of the debt as of December 31, 20X1. The lender waives ~~that~~its right to demand payment of the debt for this specific violation for a period greater than one year after the balance sheet date ~~but~~and retains the other future covenant requirements. The lender issues the waiver to the borrower after the balance sheet date but before the borrower's financial statements are issued. The borrower pays a fee to the lender to receive the waiver. There is no change to the interest rate, duration of the loan, or other terms of the debt agreement.

470-10-55-3A The borrower assesses the criteria in paragraph 470-10-45-23 to determine whether the debt should be classified as a noncurrent liability on its classified balance sheet. The borrower determines that the criteria in paragraph 470-10-45-23(a) through (b) have been met because the debt would have been classified as noncurrent absent the covenant violation, the waiver was obtained before the financial statements were issued, and the waiver is for a period greater than one year after the balance sheet date. The borrower determines that the criterion in paragraph 470-10-45-23(c) has been met because the waiver received did not result in an extinguishment under Subtopic 470-50 or a troubled debt restructuring under Subtopic 470-60. In granting the waiver, the only change to the debt arrangement is the payment of a fee. The amount of the fee changed the present value of cash flows under the terms of the original instrument less than 10 percent, indicating that the payment of the fee did not result in an extinguishment of the debt. The borrower determines that the criterion in paragraph 470-10-45-23(d) has been met because it is not probable that the borrower will violate any other covenant within 12 months from the balance sheet date.

470-10-55-3B The borrower presents in a separate line item on its balance sheet the amount of debt that is classified as a noncurrent liability because of the application of guidance in paragraphs 470-10-45-23 through 45-24. The borrower also complies with the disclosure requirements in paragraph 470-10-50-6.

> > > Case B: Debt Is Classified as Noncurrent (Subsequent Event)

470-10-55-3C Assume the same facts as in Case A, except that the borrower violates the covenant at the March 31, 20X2 compliance date (after being in compliance with the covenant at December 31, 20X1). The borrower issues its December 31, 20X1 financial statements in April 20X2.

470-10-55-3D The borrower determines that the violation of the covenant is a nonrecognized subsequent event (as described in paragraph 855-10-25-3) for the December 31, 20X1 financial statements because the event provides evidence about conditions that arose after the balance sheet date. Therefore, the debt is classified as a noncurrent liability on the borrower's classified balance sheet for the period ended December 31, 20X1, on the basis of the guidance in paragraph 470-10-45-22. The borrower provides disclosures about the nonrecognized subsequent event in accordance with the requirements in paragraph 855-10-50-2.

> > > Case C: Debt Is Classified as Current (Extinguishment)

470-10-55-3E Assume the same facts as Case A (the borrower violates a covenant as of December 31, 20X1), except that in granting the waiver the lender modifies the debt arrangement to increase the borrower's interest rate. The borrower concludes that the modification does not result in a troubled debt restructuring under Subtopic 470-60. However, the borrower concludes that the criterion in paragraph 470-10-45-23(c) has not been met because the modification should be accounted for as an extinguishment under Subtopic 470-50 because the increase in the interest rate changed the present value of cash flows under the terms of the original instrument by at least 10 percent. Thus, the borrower classifies the debt as a current liability as of December 31, 20X1, in its classified balance sheet.

> > > Case D: Debt Is Classified as Current (Probability Assessment)

470-10-55-3F Assume the same facts as Case A (the borrower violates a covenant as of December 31, 20X1), except that in this case it is probable that another covenant will be violated within 12 months from the balance sheet date. Because the criterion in paragraph 470-10-45-23(d) has not been met, the borrower classifies the debt as a current liability as of December 31, 20X1, in its classified balance sheet.

470-10-55-4 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~The issue is whether the waiver of the lender's rights resulting from the violation of the covenant with the retention of the periodic covenant tests represents, in substance, a grace period. If viewed as a grace period, the borrower would classify the debt as current (see paragraph 470-10-45-11) unless it is probable that the borrower can cure the violation (comply with the covenant) within the grace period. Specifically, the balance sheet classification of an obligation is considered in the following situations:~~

~~a. The debt covenants are applicable only after the balance sheet date, and it is probable that the borrower will fail to meet the covenant requirement at the compliance date three months after the balance sheet date.~~

~~b. The borrower meets the current covenant requirement at the balance sheet date, and it is probable that the borrower will fail to meet the same covenant requirement at the compliance date in three months.~~

~~c. The borrower meets the current covenant requirement, and it is probable that the borrower will fail to meet a more restrictive covenant requirement applicable at the compliance date in three months.~~

~~d. The borrower has met the covenant requirement in the prior quarter but before the balance sheet date negotiates a modification of the loan agreement that eliminates the covenant requirements at the balance sheet date or modifies the requirement so that the borrower will comply. Absent the modification, the borrower would have been in violation of the covenant at the balance sheet date. The same or a more restrictive covenant must be met at the compliance date in three months, and it is probable that the borrower will fail to meet that requirement at that subsequent date.~~

~~e. The borrower is in violation of the current covenant requirement at the balance sheet date and, after the balance sheet date but before the financial statements are issued or available to be issued (as discussed in Section 855-10-25), obtains a waiver. The same or a more restrictive covenant must be met at the compliance date in three months, and it is probable that the borrower will fail to meet that requirement at that subsequent date.~~

470-10-55-5 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~In the situations described in (a) through (c) of the preceding paragraph, the debt would be classified as noncurrent, in which case the borrower would be required to disclose the adverse consequences of its probable failure to satisfy future covenants.~~

470-10-55-6 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~In the situations described in paragraph 470-10-55-4(d) through (e), the debt would be classified as current. However, if the debt is expected to be refinanced on a long-term basis and the borrower meets the provisions of paragraphs 470-10-45-13 through 45-20, the debt would be classified as noncurrent.~~

> > Example 2: Classification by the Issuer of Redeemable Instruments That Are Subject to Remarketing Agreements

470-10-55-7 This Example illustrates the guidance for the appropriate classification by the issuer of debt if all of the following conditions exist:

a. The debt has a long-term maturity (for example, 30 to 40 years).
b. The debt holder may redeem or ~~put~~<u>demand repayment of</u> the bond on short notice (7 to 30 days).
c. The issuer has a remarketing agreement that states that the <u>third-party</u> agent will make its best effort to remarket the bond when redeemed.

d. The debt is secured by a short-term letter of credit that provides protection to the debt holder in the event that the redeemed debt cannot be remarketed. (Amounts drawn against the letter of credit are payable back to the issuer of the letter of credit by the issuer of the redeemable debt instrument~~ on the same day that the drawdown occurs~~.) The borrower obtains the letter of credit at the inception of the debt arrangement.

470-10-55-8 Debt agreements that allow a debt holder to redeem (or ~~put~~demand payment of) a debt instrument on demand (or within one year, or **operating cycle**, if longer) should be classified as short-term liabilities because none of the criteria for noncurrent classification in paragraph 470-10-45-22 have been met~~despite the existence of a best-efforts remarketing agreement. That is, unless the issuer of the redeemable debt instrument has the ability and intent to refinance the debt on a long-term basis as provided for in paragraph 470-10-45-14, the debt should be classified as a current liability~~.

470-10-55-9 In this Example, the obligation would be classified by the issuer as noncurrent only if the letter-of-credit arrangement allows the borrower to defer the payment for a period of at least one year (or operating cycle, if longer)~~meets the requirements of paragraph 470-10-45-14(b)~~. The fact that the letter of credit provider is with a different party than the original debt holder is not relevant when determining the classification of the debt.

~~**> > Example 4: Current Maturity of Long-Term Debt and Notes Payable to Be Refinanced**~~

470-10-55-13 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~The following Cases illustrate various scenarios for refinancing the current portion of long-term debt and notes payable as discussed in paragraphs 470-10-45-13 through 45-20:~~

~~a. Entity refinances on long-term basis the current maturity of long-term debt and notes payable (Case A).~~
~~b. Laws prohibit the transfer of funds (Case B).~~
~~c. Entity issues debentures to liquidate the debt (Case C).~~
~~d. Entity negotiates a revolving credit agreement (Case D).~~
~~e. Entity negotiates a revolving credit agreement with borrowing limits (Case E).~~
~~f. Entity refinances commercial paper (Case F).~~
~~g. Case illustrates balance sheet presentation (Case G).~~

470-10-55-14 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~The Cases in this Example do not comprehend all possible circumstances and~~

~~do not include all the disclosures that would typically be made regarding long-term debt or current liabilities.~~

470-10-55-15 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~Cases A through G share all of the following assumptions:~~

- ~~a. Entity A's fiscal year-end is December 31, 19X5.~~
- ~~b. The date of issuance of the December 31, 19X5, financial statements is March 31, 19X6; the Entity's practice is to issue a classified balance sheet.~~
- ~~c. At December 31, 19X5, short-term obligations include $5,000,000 representing the portion of 6 percent long-term debt maturing in February 19X6 and $3,000,000 of 9 percent notes payable issued in November 19X5 and maturing in July 19X6.~~
- ~~d. The Entity intends to refinance on a long-term basis both the current maturity of long-term debt and the 9 percent notes payable.~~
- ~~e. Accounts other than the long-term debt maturing in February 19X6 and the notes payable maturing in July 19X6 are as follows.~~

~~Current assets~~	~~$30,000,000~~
~~Other assets~~	~~$50,000,000~~
~~Accounts payable and accruals~~	~~$10,000,000~~
~~Other long-term debt~~	~~$25,000,000~~
~~Shareholders' equity~~	~~$37,000,000~~

- ~~f. Unless otherwise indicated, the Cases also assume that the lender or prospective lender is expected to be capable of honoring the agreement, that there is no evidence of a violation of any provision, and that the terms of borrowings available under the agreement are readily determinable.~~

~~> > > Case A: Entity Refinances on Long-Term Basis the Current Maturity of Long-Term Debt and Notes Payable~~

470-10-55-16 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~The Entity negotiates a financing agreement with a commercial bank in December 19X5 for a maximum borrowing of $8,000,000 at any time through 19X7 with the following terms:~~

- ~~a. Borrowings are available at Entity A's request for such purposes as it deems appropriate and will mature three years from the date of borrowing.~~
- ~~b. Amounts borrowed will bear interest at the bank's prime rate.~~

c. ~~An annual commitment fee of 1/2 of 1 percent is payable on the difference between the amount borrowed and $8,000,000.~~

d. ~~The agreement is cancelable by the lender only if any of the following occur:~~

1. ~~The Entity's **working capital**, excluding borrowings under the agreement, falls below $10,000,000.~~
2. ~~The Entity becomes obligated under lease agreements to pay an annual rental in excess of $1,000,000.~~
3. ~~Treasury stock is acquired without the prior approval of the prospective lender.~~
4. ~~The Entity guarantees indebtedness of unaffiliated persons in excess of $500,000.~~

470-10-55-17 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~The Entity's intention to refinance meets the condition specified by paragraph 470-10-45-14. Compliance with the provisions listed in (d) of the preceding paragraph is objectively determinable or measurable; therefore, the condition specified by paragraph 470-10-45-14(b)(1) is met. The proceeds of borrowings under the agreement are clearly available for the liquidation of the 9 percent notes payable and the long-term debt maturing in February 19X6. Both obligations, therefore, would be classified as other than current liabilities.~~

470-10-55-18 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~Following are the liability section of Entity A's balance sheet at December 31, 19X5, and the related note disclosures required by this Subtopic, based on the information in paragraphs 470-10-55-15 through 55-16. Because the balance sheet is issued subsequent to the February 19X6 maturity of the long-term debt, the note describes the refinancing of that obligation.~~

	~~**December 31, 19X5**~~	
~~Current Liabilities:~~		
~~Accounts payable and accruals~~	~~$ 10,000,000~~	
~~Total Current Liabilities~~	~~10,000,000~~	
~~Long-Term Debt:~~		
~~9% notes payable (Note A)~~	~~3,000,000~~	~~(a)~~
~~6% debt due February 19X6 (Note A)~~	~~5,000,000~~	~~(a)~~
~~Other long-term debt~~	~~25,000,000~~	
~~Total Long-Term Debt~~	~~33,000,000~~	
~~Total Liabilities~~	~~$ 43,000,000~~	

~~(a) These obligations may also be shown in captions distinct from both current liabilities and long-term debt, such as Interim Debt, Short-Term Debt Expected to Be Refinanced, and Intermediate Debt.~~

~~Note A~~

~~The Entity has entered into a financing agreement with a commercial bank that permits the Entity to borrow at any time through 19X7 up to $8,000,000 at the bank's prime rate of interest. The Entity must pay an annual commitment fee of 1/2 of 1 percent of the unused portion of the commitment. Borrowings under the financing agreement mature three years after the date of the loan. Among other things, the agreement prohibits the acquisition of treasury stock without prior approval by the bank, requires maintenance of working capital of $10,000,000 exclusive of borrowings under the agreement, and limits the annual rental under lease agreements to $1,000,000. In February 19X6, the Entity borrowed $5,000,000 at 8 percent and liquidated the 6 percent long-term debt, and it intends to borrow additional funds available under the agreement to refinance the 9 percent notes payable maturing in July 19X6.~~

~~> > > Case B: Laws Prohibit the Transfer of Funds~~

470-10-55-19 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~A foreign subsidiary of the Entity negotiates a financing agreement with its local bank in December 19X5. Funds are available to the subsidiary for its unrestricted use, including loans to affiliated entities; other terms are identical to those cited in Case A. Local laws prohibit the transfer of funds outside the country.~~

470-10-55-20 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~The requirement of paragraph 470-10-45-14(b)(1) is met because compliance with the provisions of the agreement is objectively determinable or measurable. Because of the laws prohibiting the transfer of funds, however, the proceeds from borrowings under the agreement are not available for liquidation of the debt maturing in February and July 19X6. Accordingly, both the 6 percent debt maturing in February 19X6 and the 9 percent notes payable maturing in July 19X6 would be classified as current liabilities.~~

~~> > > Case C: Entity Issues Debentures to Liquidate the Debt~~

470-10-55-21 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~In this Case, the Entity issues $8,000,000 of 10-year debentures to the public in January 19X6. The Entity intends to use the proceeds to liquidate the $5,000,000 debt maturing February 19X6 and the $3,000,000 of 9 percent notes payable maturing July 19X6. In addition, assume the debt maturing February 19X6 is paid before the issuance of the balance sheet, and the remaining proceeds from the sale of debentures are invested in a U.S. Treasury note maturing the same day as the 9 percent notes payable.~~

470-10-55-22 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~Because the Entity refinanced the long-term debt maturing in February 19X6 in a manner that meets the conditions set forth in paragraph 470-10-45-14, that obligation would be excluded from current liabilities. In addition, the 9 percent notes payable maturing in July 19X6 would also be excluded because the Entity has obtained funds expressly intended to be used to liquidate those notes and not intended to be used in current operations. In balance sheets after the date of sale of the debentures and before the maturity date of the notes payable, the Entity would exclude the notes payable from current liabilities if the U.S. Treasury note is excluded from current assets (see paragraph 210-10-45-4).~~

470-10-55-23 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~If the debentures had been sold before January 1, 19X6, the $8,000,000 of obligations to be paid would be excluded from current liabilities in the balance sheet at that date if the $8,000,000 in funds were excluded from current assets.~~

470-10-55-24 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~If, instead of issuing the 10-year debentures, the Entity had issued $8,000,000 of equity securities and all other facts in this Case remained unchanged, both the 6 percent debt due February 19X6 and the 9 percent notes payable due July 19X6 would be classified as liabilities other than current liabilities, such as Indebtedness Due in 19X6 Refinanced in January 19X6.~~

~~> > > Case D: Revolving Credit Agreement~~

470-10-55-25 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~In December 19X5 the Entity negotiates a revolving credit agreement providing for unrestricted borrowings up to $10,000,000. Borrowings will bear interest at 1 percent over the prevailing prime rate of the bank with which the agreement is arranged but in any event not less than 8 percent, will have stated maturities of 90 days, and will be continuously renewable for 90-day periods at the Entity's option for 3 years provided there is compliance with the terms of the agreement. Provisions of the agreement are similar to those cited in paragraph 470-10-55-16(d). Further, the Entity intends to renew obligations incurred under the agreement for a period extending beyond one year from the balance sheet date. There are no outstanding borrowings under the agreement at December 31, 19X5.~~ **[Content amended and moved to paragraph 470-10-55-39]**

470-10-55-26 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~In this instance, the long-term debt maturing in February 19X6 and the 9 percent notes payable maturing in July 19X6 would be excluded from current liabilities because the Entity consummated a financing agreement meeting the conditions set forth in paragraph 470-10-45-14(b) before the issuance of the balance sheet.~~

~~**> > > Case E: Revolving Credit Agreement with Borrowing Limits**~~

470-10-55-27 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~Assume that the agreement cited in Case D included an additional provision limiting the amount to be borrowed by the Entity to the amount of its inventory, which is pledged as collateral and is expected to range between a high of $8,000,000 during the second quarter of 19X6 and a low of $4,000,000 during the fourth quarter of 19X6.~~

470-10-55-28 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~The terms of the agreement comply with the conditions required by this Subtopic; however, because the minimum amount expected to be available from February to December 19X6 is $4,000,000, only that amount of short-term obligations can be excluded from current liabilities (see paragraphs 470-10-45-16 through 45-19). Whether the obligation to be excluded is a portion of the currently maturing long-term debt or some portions of both it and the 9 percent notes payable depends on the intended timing of the borrowing.~~

470-10-55-29 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~If the Entity intended to refinance only the 9 percent notes payable due July 19X6 and the amount of its inventory is expected to reach a low of approximately $2,000,000 during the second quarter of 19X6 but be at least $3,000,000 in July 19X6 and thereafter during 19X6, the $3,000,000 9 percent notes payable would be excluded from current liabilities at December 31, 19X5 (see paragraphs 470-10-45-16 through 45-19).~~

~~**> > > Case F: Commercial Paper Refinancing**~~

470-10-55-30 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~In lieu of the facts given in paragraph 470-10-55-15(c) through (d), assume that during 19X5 the Entity entered into a contract to have a warehouse built. The warehouse is expected to be financed by issuance of the Entity's commercial paper. In addition, the Entity negotiated a standby agreement with a commercial bank that provides for maximum borrowings equal to the expected cost of the warehouse, which will be pledged as collateral. The agreement also requires that the proceeds from the sale of commercial paper be used to pay construction costs. Borrowings may be made under the agreement only if the Entity is unable to issue new commercial paper. The proceeds of borrowings must be used to retire outstanding commercial paper and to liquidate additional liabilities incurred in the construction of the warehouse. At December 31, 19X5, the Entity has $7,000,000 of commercial paper outstanding and $1,000,000 of unpaid construction costs resulting from a progress billing through December 31.~~

470-10-55-31 <u>Paragraph superseded by Accounting Standards Update No. 201X-XX.</u>~~Because the commercial paper will be refinanced on a long-term basis, either~~

~~by uninterrupted renewal or, failing that, by a borrowing under the agreement, the commercial paper would be excluded from current liabilities. The $1,000,000 liability for the unpaid progress billing results from the construction of a noncurrent asset and will be refinanced on the same basis as the commercial paper and, therefore, it would also be excluded from current liabilities (see paragraph 470-10-45-13).~~

~~> > > Case G: Balance Sheet Presentation~~

470-10-55-32 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~The following are two methods of presenting liabilities in Entity A's balance sheet at December 31, 19X5, assuming the Entity intends to refinance the 6 percent debt maturing in February 19X6 and the 9 percent notes payable maturing in July 19X6 but has not met the conditions required by this Subtopic to exclude those obligations from current liabilities.~~

~~**Alternative 1**~~

	~~**December 31, 19X5**~~
~~Current Liabilities:~~	
~~Accounts payable and accruals~~	~~$ 10,000,000~~
~~Notes payable, due July 19X6~~	~~3,000,000~~
~~6% debt due February 19X6~~	~~5,000,000~~
~~Total Current Liabilities~~	~~18,000,000~~
~~Long-Term Debt~~	~~25,000,000~~
~~Total Liabilities~~	~~$ 43,000,000~~

~~**Alternative 2**~~

		~~**December 31, 19X5**~~
~~Current Liabilities:~~		
~~Accounts payable and accruals~~		~~$ 10,000,000~~
~~Short-term debt expected to be refinanced:~~		
~~Notes payable, due July 19X6~~	~~$ 3,000,000~~	
~~6% debt due February 19X6~~	~~5,000,000~~	~~8,000,000~~
~~Total Current Liabilities~~		~~18,000,000~~
~~Long-Term Debt~~		~~25,000,000~~
~~Total Liabilities~~		~~$ 43,000,000~~

~~> > Example 5: Classification of a Short-Term Obligation Repaid Before Being Replaced by a Long-Term Security~~

470-10-55-33 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~This Example illustrates the guidance in paragraph 470-10-45-15.~~

470-10-55-34 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~This Example has the following assumptions:~~

a. ~~An Entity has issued $3,000,000 of short-term commercial paper during the year to finance construction of a plant.~~
b. ~~At June 30, 1976, the Entity's fiscal year end, the Entity intends to refinance the commercial paper by issuing long-term debt. However, because the Entity temporarily has excess cash, in July 1976 it liquidates $1,000,000 of the commercial paper as the paper matures.~~
c. ~~In August 1976, the Entity completes a $6,000,000 long-term debt offering.~~
d. ~~Later during the month of August, it issues its June 30, 1976, financial statements.~~
e. ~~The proceeds of the long-term debt offering are to be used to do all of the following:~~
    1. ~~Replenish $1,000,000 in working capital~~
    2. ~~Pay $2,000,000 of commercial paper as it matures in September 1976~~
    3. ~~Pay $3,000,000 of construction costs expected to be incurred later that year to complete the plant.~~

470-10-55-35 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~The $1,000,000 of commercial paper liquidated in July would be classified as a current liability in the Entity's balance sheet at June 30, 1976. The $2,000,000 of commercial paper liquidated in September 1976 but refinanced by the long-term debt offering in August 1976 would be excluded from current liabilities in balance sheets at the end of June 1976, July 1976, and August 1976. It should be noted that the existence of a financing agreement at the date the financial statements are issued or are available to be issued (as discussed in Section 855-10-25) rather than a completed financing at that date would not change these classifications.~~

470-10-55-36 Paragraph superseded by Accounting Standards Update No. 201X-XX.~~At the end of August 1976, $2,000,000 of cash would be excluded from current assets or, if included in current assets, a like amount of debt would be classified as a current liability.~~

> > Example 6: Short-Term Debt Refinanced on a Long-Term Basis

470-10-55-37 As of December 31, 20X1, the borrower has a loan outstanding that is due on June 30, 20X2. In February 20X2, the borrower refinances the debt resulting in a new due date of June 30, 20X4. The borrower issues its financial statements on March 30, 20X2.

470-10-55-38 The borrower assesses the criteria in paragraph 470-10-45-22 and determines that neither criterion has been met because as of December 31, 20X1, the debt is contractually due in six months and the entity does not have a contractual right to defer settlement for at least one year. Therefore, the borrower classifies the debt as current in its December 31, 20X1 financial statements. The borrower also provides disclosures about the refinancing in accordance with the requirements in paragraph 855-10-50-2.

> > Example 7: Revolving Credit Agreement

470-10-55-39 In December ~~19X5~~20X5 the ~~Entity~~borrower negotiates a revolving credit agreement providing for unrestricted borrowings up to $10,000,000. Borrowings will bear interest at 1 percent over the prevailing prime rate of the bank with which the agreement is arranged but in any event not less than 8 percent, will have stated maturities of 90 days, and will be continuously renewable for 90-day periods at the ~~Entity's~~borrower's option for 3 years provided there is compliance with the terms of the agreement. As of December 31, 20X5, the borrower has drawn down $500,000 against this revolving credit agreement.~~Provisions of the agreement are similar to those cited in paragraph 470-10-55-16(d). Further, the Entity intends to renew obligations incurred under the agreement for a period extending beyond one year from the balance sheet date. There are no outstanding borrowings under the agreement at December 31, 19X5.~~ **[Content amended as shown and moved from paragraph 470-10-55-25]**

470-10-55-40 The borrower considers the criteria in paragraph 470-10-45-22 in determining the classification of the $500,000 of debt outstanding in its classified balance sheet. Although the revolving credit agreement fails to meet criterion (a) because of the 90-day maturities, the borrower determines that it has met criterion (b) because the borrower has the contractual right to defer settlement for 3 years. Therefore, the borrower classifies the debt as a noncurrent liability in its classified balance sheet.

> > Example 8: Subjective Acceleration Clause

> > > Case A: Debt Is Classified as a Noncurrent Liability

470-10-55-41 The borrower has a loan outstanding that is due in five years. The loan agreement stipulates that if a circumstance has occurred that would reasonably be expected to have a material adverse effect upon the business, operations, properties, assets, or condition of the borrower, then the loan is in default. As of the end of the reporting period, the borrower has not received any notification from the lender that it is not in compliance with this clause. The borrower determines that both criteria in paragraph 470-10-45-22 have been met. Therefore, the borrower classifies the debt as a noncurrent liability on its classified balance sheet.

> > > Case B: Debt Is Classified as Current with Disclosures

470-10-55-42 Assume the same facts in Case A. In addition, assume that in the fourth quarter of the reporting period, the borrower has lost an essential customer that accounts for more than 10 percent of its sales. In December of that reporting year, the lender notifies the borrower of noncompliance with the material adverse change clause of its debt arrangement.

470-10-55-43 Because the lender has notified the borrower of an event of default, the debt fails to meet the criteria in paragraph 470-10-45-22. Therefore, the borrower classifies the debt as a current liability in its classified balance sheet. The borrower provides the disclosures required in paragraph 470-10-50-6.

> > Example 9: Objectively Determinable Clause—Borrowing Base

470-10-55-44 A borrower enters into a debt agreement for $2 million due in 3 years. The debt agreement stipulates that if the amount outstanding on the debt exceeds the borrowing base (the calculation of which is prescribed in the debt agreement), the amount in excess of the borrowing base is due and payable within five months of the borrowing base redetermination date (that is, the date at which the borrowing base calculation is performed).

470-10-55-45 Assume that at December 31, 20X1, the amount of outstanding debt does not exceed the borrowing base. In this case, the borrower would meet the criteria in paragraph 470-10-45-22 because the debt is due in three years. The borrower would classify the debt as a noncurrent liability in its classified balance sheet. However, if all or a portion of the outstanding debt as of the balance sheet date exceeds the borrowing base at the balance sheet date, the borrower would classify that portion of the debt that would be due in less than one year as a current liability. The remainder of the debt would be classified as a noncurrent liability in the borrower's classified balance sheet because it would meet the criteria in paragraph 470-10-45-22.

9. Add paragraph 470-10-65-1 and its related heading as follows:

> Transition Related to Accounting Standards Update No. 201X-XX, *Debt (Topic 470): Simplifying the Classification of Debt in a Classified Balance Sheet (Current versus Noncurrent)*

470-10-65-1 The following represents the transition and effective date information related to Accounting Standards Update No. 201X-XX, *Debt (Topic 470): Simplifying the Classification of Debt in a Classified Balance Sheet (Current versus Noncurrent)*:

a. The pending content that links to this paragraph shall be effective for fiscal years beginning after [date to be inserted after exposure], and interim periods within or after those fiscal years [timing of interim period adoption to be inserted after exposure]. Earlier adoption is permitted.

b. An entity shall apply the pending content that links to this paragraph prospectively to all **debt arrangements**, **mandatorily redeemable financial instruments** within the scope of Topic 480 on distinguishing liabilities from equity, and debt with conversion and other options that are within the scope of Subtopic 470-20 that exist as of the date of initial adoption.

c. An entity is required to disclose the following in the first interim and annual period of adoption:
   1. The nature of and reason for the change in accounting principle
   2. The effect of the change on the affected financial statement line items in the current period.

Amendments to Subtopic 210-10

10. Amend paragraphs 210-10-45-7 and 210-10-45-12, with a link to transition paragraph 470-10-65-1, as follows:

Balance Sheet—Overall

Other Presentation Matters

> Classification of Current Liabilities

210-10-45-5 A total of **current liabilities** shall be presented in classified balance sheets.

210-10-45-6 The concept of current liabilities includes estimated or accrued amounts that are expected to be required to cover expenditures within the year for known obligations the amount of which can be determined only approximately (as in the case of provisions for accruing bonus payments) or where the specific person or persons to whom payment will be made cannot as yet be designated (as in the case of estimated costs to be incurred in connection with guaranteed servicing or repair of products already sold).

210-10-45-7 Section 470-10-45 includes guidance on the classification of a **debt arrangement**, a liability-classified **mandatorily redeemable financial instrument** within the scope of Subtopic 480-10 on distinguishing liabilities from equity, and debt with conversion and other options that are within the scope of Subtopic 470-20.~~various debt transactions that may result in current liability classification. These transactions are the following:~~

a. Subparagraph superseded by Accounting Standards Update No. 201X-XX.~~Due-on-demand loan agreements.~~
b. Subparagraph superseded by Accounting Standards Update No. 201X-XX~~Callable debt agreements.~~
c. Subparagraph superseded by Accounting Standards Update No. 201X-XX~~**Short-term obligations** expected to be refinanced.~~

> > Other Liabilities

210-10-45-12 The current liability classification is not intended to include ~~debts~~ liabilities to be liquidated by funds that have been accumulated in accounts of a type not properly classified as current assets, or long-term obligations incurred to provide increased amounts of **working capital** for long periods.

Amendments to Subtopic 470-20

11. Add paragraph 470-20-45-2B and its related heading and amend paragraph 470-20-45-3, with a link to transition paragraph 470-10-65-1, as follows:

Debt—Debt with Conversion and Other Options

Other Presentation Matters

General

> Balance Sheet Classification

470-20-45-2B See Subtopic 470-10 for guidance on classifying instruments within the scope of this Subtopic as current liabilities or noncurrent liabilities.

Cash Conversion

> Balance Sheet Classification of Liability Component

470-20-45-3 The guidance in the Cash Conversion Subsections does not affect an issuer's determination of whether the liability component should be classified as a current liability or a ~~long-term~~noncurrent liability (see paragraph 470-20-45-2B). ~~For purposes of applying other applicable U.S. GAAP to~~To make that determination, an entity shall consider all terms of the convertible debt instrument (including the equity component)~~ shall be considered~~. Additionally, the balance sheet classification of the liability component does not affect the measurement of that component under paragraphs 470-20-35-12 through 35-16.

Amendments to Subtopic 480-10

12. Add paragraph 480-10-45-5 and its related heading, with a link to transition paragraph 470-10-65-1, as follows:

Distinguishing Liabilities from Equity—Overall

Other Presentation Matters

> Balance Sheet Classification (Current Liabilities or Noncurrent Liabilities)

480-10-45-5 See Subtopic 470-10 on debt for guidance on classifying a liability-classified **mandatorily redeemable financial instrument** within the scope of this Subtopic as current liabilities or noncurrent liabilities.

Amendments to Subtopic 852-10

13. Amend paragraph 852-10-45-8, with a link to transition paragraph 470-10-65-1, as follows:

Reorganizations—Overall

Other Presentation Matters

> Financial Reporting During Reorganization Proceedings

> > Balance Sheet

852-10-45-8 Paragraph 470-10-45-22~~Section 470-10-45~~ requires current liabilities classification in a classified balance sheet for long-term liabilities that, by their terms, are due on demand or will be due on demand within one year, or the operating cycle, if longer. Current liabilities classification is required because those liabilities do not meet the criteria in paragraph 470-10-45-22. This classification requirement also applies to long-term liabilities that are or will be callable by the creditor because of a violation of a provision of the debt agreement. The **automatic stay provisions** of Chapter 11 make it unnecessary to reclassify prepetition long-term liabilities even though prepetition creditors might demand payment or there is a violation of a covenant in the debt agreement.

Amendments to Subtopic 855-10

14. Amend paragraph 855-10-15-5, with a link to transition paragraph 470-10-65-1, as follows:

Subsequent Events—Overall

Scope and Scope Exceptions

> Transactions

855-10-15-5 The following are examples (not collectively exhaustive) of other subsequent events guidance that is not consistent with the principles in this Topic for the recognition and disclosure of events or transactions that occur after the balance sheet date.

a. Income Taxes—See paragraph 740-10-25-15 for guidance on changes in judgment after the balance sheet date that results in subsequent recognition, derecognition, or change in measurement of a tax position taken in a prior annual period.
b. Earnings per Share—See paragraph 260-10-55-12 for guidance on the effect on earnings per share of changes in the number of common shares as a result of a stock dividend or stock split that occurs after the balance sheet date but before the financial statements are issued or are available to be issued.
c. Gain Contingencies—See paragraph 450-30-25-1 for guidance on gain contingencies which are rarely recognized after the balance sheet date but before the financial statements are issued or are available to be issued.
d. Debt Presentation—See paragraph 470-10-45-23 for guidance on a waiver of a debt covenant violation obtained by a borrower after the reporting date but before the financial statements are issued (or are available to be issued).

The amendments in this proposed Update were approved for publication by the unanimous vote of the seven members of the Financial Accounting Standards Board:

Russell G. Golden, *Chairman*
James L. Kroeker, *Vice Chairman*
Christine A. Botosan
Daryl E. Buck
R. Harold Schroeder
Marc A. Siegel
Lawrence W. Smith

Background Information and Basis for Conclusions

Introduction

BC1. The following summarizes the Board's considerations in reaching the conclusions in this proposed Update. It includes reasons for accepting certain approaches and rejecting others. Individual Board members gave greater weight to some factors than to others.

BC2. The Board is issuing this proposed Update as part of its Simplification Initiative. The objective of the Simplification Initiative is to identify, evaluate, and improve areas of GAAP for which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to users of financial statements.

Background Information

BC3. Current guidance includes a variety of rules that apply to different types of debt arrangements to determine whether amounts should be classified as current liabilities or noncurrent liabilities in a classified balance sheet. For example, separate guidance exists for callable debt, debt due on demand, debt with covenant violations, short-term debt refinanced on a long-term basis, debt with lockboxes, debt with springing lockboxes, and so forth. That guidance is disparate and at times inconsistent because the separate guidance was developed individually, in response to specific facts and circumstances, over a long period of time. The objective of this project is to introduce an overarching, cohesive principle for determining whether debt should be classified as current or noncurrent that will reduce the cost and complexity of applying the guidance and improve the usefulness of the information reported to financial statement users.

BC4. In addition to the classification guidance in Topic 470, entities also refer to the definition of the term *current liabilities* in the Master Glossary and presentation guidance in Topic 210, Balance Sheet. The term *noncurrent liability* is not explicitly defined in current GAAP, but in practice a noncurrent liability is a liability that does not meet the definition of current liabilities.

Benefits and Costs

BC5. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Board's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC6. The Board anticipates that the benefits of the amendments in this proposed Update would justify the costs. The current guidance on determining when debt should be classified as a current liability or a noncurrent liability in the balance sheet is difficult for preparers and auditors to navigate and for financial statement users to understand. The Board expects that the determination under the proposed amendments would be simpler than under current GAAP. The Board also expects that the proposed amendments would benefit financial statement users by providing greater transparency about the nature of the debt that is classified as a noncurrent liability in the balance sheet. During outreach with financial statement users, many were unaware of the labyrinth of rules that exists today.

BC7. The Board also concluded that a classified balance sheet prepared under current GAAP does not sufficiently depict liquidity when an entity has (a) violated a debt covenant and received a subsequent waiver or (b) subsequently refinanced short-term debt on a long-term basis. In both of those cases, debt is presented as a noncurrent liability under current guidance. Current GAAP does not require separate presentation or specific disclosures that would highlight those circumstances for financial statement users. The Board expects that the amendments in this proposed Update would benefit financial statement users by providing greater transparency and consistency in the types of debt that are classified as noncurrent liabilities in the balance sheet. As such, the Board expects that the resulting information will be more understandable to financial statement users.

BC8. During this project, the staff discussed the amendments in this proposed Update and alternatives with advisory members at meetings of the Private Company Council (PCC), the FASB's Small Business Advisory Committee (SBAC), and the FASB's Investor Advisory Committee (IAC). The staff also conducted outreach with other stakeholders, including private company financial statement users. Some stakeholders (including some members of the PCC and the SBAC) had raised concerns about the effect of the Board's decisions in cases in which the principle would result in an increase in current liabilities, as compared with a classified balance sheet prepared using current guidance. In those cases, stakeholders raised concerns about a change in the amount of current liabilities triggering a debt covenant violation. A debt covenant violation could affect an entity's ability to obtain future financing or its ability to meet other licensing requirements, such as the requirements for construction contractors. The Board observes that the proposed amendments would not affect an entity's total debt position. Rather, the proposed amendments would provide increased transparency about an entity's debt arrangements. Therefore, the Board does not expect an entity to incur significant costs solely because the entity implements the amendments in this proposed Update.

Scope

BC9. The Board decided that the amendments in this proposed Update would apply to all debt arrangements as well as convertible debt and liability-classified mandatorily redeemable financial instruments that are classified as liabilities. The proposed amendments include the following definition of a debt arrangement:

> An arrangement that provides a lender with a contractual right to receive consideration and a borrower with a contractual obligation to pay consideration on demand or on fixed or determinable dates.

BC10. The Master Glossary had included a definition of the term *debt*. The Board removed that glossary term in Accounting Standards Update No. 2016-19, *Technical Corrections and Improvements*. That term had originated from FASB Statement No. 15, *Accounting by Debtors and Creditors for Troubled Debt Restructurings*. That definition was developed specifically for the guidance on troubled debt restructurings. The new Master Glossary term in the amendments in this proposed Update was modeled after the previous definition of debt but was modified to remove references to restructuring.

BC11. Mandatorily redeemable financial instruments that are classified as liabilities are similar to debt arrangements. Although those instruments are recorded as liabilities, they are not debt instruments because they are issued in the form of equity. However, the Board decided that the amendments in this proposed Update also should apply to liability-classified mandatorily redeemable financial instruments because of their similarities with debt arrangements, as well as the lack of specific guidance for determining whether those instruments should be classified as current liabilities or noncurrent liabilities.

BC12. Convertible debt generally would meet the definition of a debt arrangement. However, because convertible debt may be share settled, the Board decided to explicitly include those instruments within the scope of the amendments in this proposed Update to alleviate the level of questions that might develop in practice on this topic.

Classification of Debt in a Classified Balance Sheet

BC13. The Board observed inconsistencies in the current guidance in Topic 470 on determining whether to classify debt as a current liability or a noncurrent liability. Some guidance revolves around management expectations of when debt might be settled, whereas other guidance focuses on the terms and conditions of the contract. The Board decided to align the guidance under a single principle that is centered on the terms and conditions of the contract.

BC14. The Board concluded that a principle that is based on the terms and conditions of the contract (“a contractual approach”) would be more operable because the evidence is more objective than the evidence provided by management expectations. The Board expects that a contractual approach would be simpler for preparers to apply and for auditors to audit, as compared with current GAAP. During the staff’s outreach on this project, financial statement users were more supportive of a contractual approach than an approach based on management expectations. Financial statement users expressed concerns that a principle based on management expectations would be subjective and could introduce noncomparability between companies and within a company over time. For example, if two entities have the same underlying terms and conditions within a debt arrangement, each entity’s management could have different expectations about when the debt might be settled. If the classification of debt is based on management expectations, the debt could be classified as a current liability for one entity and a noncurrent liability for the other entity.

BC15. In choosing an alternative, the Board considered the consistency of its approach as compared with the definition of the term *current liabilities* in the Master Glossary, which is defined as “obligations whose liquidation is *reasonably expected* to require the use of existing resources properly classifiable as current assets, or the creation of other current liabilities” (emphasis added). Therefore, the definition of current liabilities includes consideration of management expectations. In the judgment of the Board, an entity would be unable to reasonably expect debt to be a noncurrent liability unless the entity has contractual rights that would support that expectation. For example, if an entity has debt due in six months, it would be unreasonable for management to assert that the debt is a noncurrent liability on the basis of its expectation. If management intends to refinance the debt in a subsequent period, the entity would need the lender to agree to the refinancing. Additionally, debt that is due on demand or puttable would not meet the criteria for noncurrent classification.

BC16. The amendments in this proposed Update would make GAAP more consistent with International Financial Reporting Standards (IFRS). IAS 1, *Presentation of Financial Statements,* includes guidance on the classification of liabilities. The Board leveraged IAS 1 guidance when developing its proposal for the classification of debt. However, differences would still remain between GAAP and IFRS for the classification of debt arrangements with covenant violations. IAS 1 prohibits entities from considering a waiver of debt covenant violations granted after the reporting date for purposes of determining the classification of the debt, whereas GAAP would require entities to consider waivers obtained after the reporting date but before the financial statements are issued (or are available to be issued).

BC17. The International Accounting Standards Board (IASB) currently has a project on its agenda to amend IAS 1, specifically related to the classification of liabilities. The IASB issued its Exposure Draft, *Classification of Liabilities,* in February 2015 and in December 2015 discussed an analysis of the comment letters received on that proposal. The Board considered the IASB's proposed amendments in developing the amendments in this proposed Update and will continue to monitor the IASB's ongoing project.

BC18. PCC members provided feedback to the Board on the proposed principle throughout the project. PCC members provided mixed views on the classification principle. Some members supported the Board's decisions of a classification principle and an exception for waivers of debt covenant violations. Some members supported the retention of current GAAP in its entirety and the removal of the project from the Board's agenda. Some members supported an adjustment of the scope of the project to focus on targeted areas (but retain current GAAP for post-balance-sheet refinancings). Lastly, some members recommended that the Board holistically reexamine classification in the balance sheet for all assets and liabilities. The majority of financial statement users on the PCC supported the Board's decision to pursue a classification principle with an exception for waivers of debt covenant violations. PCC members also supported the classification of debt with subjective acceleration clauses under the proposed principle. That is, they supported the subjective acceleration clause affecting classification of debt only upon trigger and the removal of the probability assessment that exists in current GAAP.

BC19. The Board considered the *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies* in determining whether the requirements for private companies should be the same as those for other entities. According to the Private Company Decision-Making Framework, generally both private and public entities should apply the same financial statement display (the term *display* is synonymous with the term *presentation*) guidance established by the Board. There is a presumption in the Private Company Decision-Making Framework that information that is important enough to be presented on the face of financial statements is relevant to most financial statement users. However, in some circumstances, the Board and the PCC may conclude that private companies should be permitted to apply alternative display requirements. In determining whether to permit a display alternative, the Private Company Decision-Making Framework describes some of the pertinent considerations that the Board and the PCC should assess. Those considerations include whether the information to be displayed is not relevant to typical users of private company financial statements, whether the information does not apply to private companies, or whether disclosing the disaggregated or supplemental information about financial statement line items in the accompanying notes would sufficiently address the needs of typical users without fundamentally affecting the comparison of financial statements of private companies and public entities. The Board determined that the classification of debt in a classified balance sheet is just as relevant to users of private company financial statements as it is to users of public company financial statements and, therefore, that a private company alternative would be inappropriate.

Subsequent Events

BC20. The Board is proposing to eliminate most scenarios in which an entity classifies debt on the basis of facts and circumstances that arise after the reporting date. Current GAAP is inconsistent in this area because at times an entity may consider events that occur after the reporting date but before the financial statements are issued (or are available to be issued) when determining whether debt should be classified as a current liability or a noncurrent liability. Topic 855, Subsequent Events, provides guidance on recognized and nonrecognized subsequent events (often referred to as Type 1 and Type 2 subsequent events, respectively). The Board observed that current guidance on the classification of debt (as current liabilities or noncurrent liabilities) allows for certain Type 2 subsequent events (for example, refinancings of debt) to be treated as Type 1 subsequent events. The amendments in this proposed Update would largely eliminate that inconsistency, except for certain waivers of violations of debt covenants.

BC21. One of the most significant changes within the amendments in this proposed Update is the exclusion of nonrecognized subsequent events in the classification of debt, specifically as it relates to subsequent refinancings of debt. Topic 470 currently requires that a short-term obligation be *excluded* from current liabilities if the entity intends to refinance the obligation on a long-term basis and is able to consummate the refinancing after the balance sheet date, but before its financial statements are issued. The proposed amendments would require a short-term obligation that is refinanced after the reporting date but before its financial statements are issued to be classified as a current liability. A short-term obligation would be a current liability because, at the reporting date, the entity would not have the right to defer settlement of the debt. The debt would be contractually due in less than 12 months.

BC22. The Board concluded that the refinancing of debt after the reporting period is a new transaction and should not be retroactively reflected in the balance sheet classification of debt. The Board views subsequent refinancings of debt differently from subsequent waivers of debt covenant violations because an entity has the discretion to renegotiate and refinance its debt before the reporting date or enter into a longer term arrangement. In contrast, an entity typically cannot obtain a waiver of debt covenant violations before the reporting date.

Waivers of Covenant Violations

BC23. The proposed amendments in paragraph 470-10-45-23 would provide an exception to the debt classification principle for certain waivers of debt covenant violations obtained after the reporting date but before financial statements are issued (or are available to be issued). Current GAAP includes a similar requirement in paragraph 470-10-45-1. The Board initially preferred an approach that would result in an entity classifying debt with a covenant violation (and with no waiver granted by the lender as of the reporting date) as a current liability. The debt is in default at the reporting date, and the Board concluded that classification of the debt as a current liability provided decision-useful information to financial statement users and more transparency on liquidity, as compared with current classification requirements. This approach would have been consistent with IFRS guidance.

BC24. However, PCC and SBAC members (before the shift of the SBAC to small public companies) observed that requiring debt with covenant violations at the reporting date to be classified as a current liability could have a significant effect on private companies. PCC members advised the Board that it may be impractical for an entity to obtain a waiver of a debt covenant violation before the reporting date. Stakeholders have explained to the Board that, generally, lenders will not issue waivers before the reporting date. General practice for debt covenant violations is that an entity provides the bank with draft financial statements for the year-end period, the lender provides a waiver after year-end, and then the entity later issues its financial statements with the debt classified as a noncurrent liability.

BC25. The Board decided to include an exception to the debt classification principle, similar to current GAAP, because of the practical difficulties. Similar requirements exist in GAAP for waivers of debt covenant violations obtained after the reporting date but before financial statements are issued. The Board decided to clarify the application of the existing guidance that requires an entity to consider the probability of other covenant violations. Specifically, the amendments in this proposed Update would require an entity to assess whether it is probable that any other covenants not covered by the waiver will be violated within 12 months (or an operating cycle, if longer) from the balance sheet date. If probable, the debt would be classified as a current liability. On the basis of outreach performed, the Board understands that many entities interpret the current guidance in this manner and, therefore, the Board expects that the effect of this proposed amendment would be limited. The Board considered whether to require a probability assessment for all debt (that is, even debt with no covenant violations) but decided that the probability assessment would only be applicable once a covenant has been violated because that debt is more likely to have subsequent violations and therefore the information would be relevant to financial statement users.

BC26. The amendments in this proposed Update include some changes to the debt classification guidance for waivers of debt covenant violations (obtained after the reporting date but before financial statements are issued or are available to be issued) as compared with current GAAP. The most significant change is the requirement for separate line item presentation in a classified balance sheet for debt that is classified as a noncurrent liability because of a waiver of a debt covenant violation received after the reporting date but before the financial statements are issued. The Board emphasized that its decision to provide an exception for such waivers was contingent on requiring an entity to separately present the amount of debt that is noncurrent because of the exception for waivers. The Board observed that the proposed exception to the principle signifies that the receipt of a waiver, after the reporting date but before financial statements are issued, is an event that is important enough to affect the classification of debt as current or noncurrent. Therefore, it should be prominently displayed on the balance sheet to provide users with a clearer picture of the entity's liquidity.

BC27. Another proposed change to current GAAP relates to waivers that result in a troubled debt restructuring or an extinguishment of debt. The amendments in this proposed Update would add new links to the guidance for troubled debt restructurings in Subtopic 470-60, Debt—Troubled Debt Restructurings by Debtors, and extinguishments of debt in Subtopic 470-50. The Board supported those proposed amendments because when the waiver results in a troubled debt restructuring or an extinguishment of debt, it is akin to the issuance of a new debt instrument. In that case, the debt as of the reporting date should be classified as a current liability because it was in default. The subsequent period would show the "new" debt arrangement that the entity entered into after the balance sheet date. That outcome is similar to the requirements for the classification of subsequent refinancings of debt under the proposed amendments. The PCC expressed its support of the proposed amendments for waivers that result in a troubled debt restructuring or an extinguishment of debt.

BC28. The Board also discussed whether to require the accrual of fees paid in conjunction with waivers of debt covenant violations. The Board decided not to amend GAAP to require accrual of those fees.

Refinancings of Debt

BC29. Some stakeholders have suggested that short-term debt should be classified as a noncurrent liability when an entity refinances that debt on a long-term basis after the reporting date but before financial statements are issued (or are available to be issued). Additionally, some PCC members had previously suggested an approach that allows for debt to be classified as a noncurrent liability when an entity refinances with the same lender (or lenders that are part of the same consolidated group). Under that approach, if the refinancing is with a different lender, the debt would be classified as a current liability. The Board rejected that approach because of the complexity and noncomparability that would be created for financial statement users if current liabilities are different amounts solely based on the identity of the lender. The Board concluded that an entity is in the same financial position both at and after the balance sheet date, regardless of whether the refinancing is consummated with a new lender or the same lender. Accordingly, the Board observes, on the basis of the amendments in this proposed Update, that if a refinancing is consummated before the balance sheet date and that refinancing allows the debt to be due in more than 12 months (or operating cycle, if longer), it is not relevant whether the refinancing agreement is with the same lender or a new lender.

BC30. Additionally, the Board has concerns that requiring a company to analyze whether it is refinancing with the same lender could introduce complexity in practice. While this would be a simple assessment when an entity is dealing with a single lender, it becomes complicated when dealing with a syndication of lenders. For example, preparers or auditors might have requested that the Board provide detailed implementation guidance on how to interpret the meaning of *same lender,* including whether the lead agent is the same, whether the lead agent is the same but one underlying lender changes, or whether half of the lenders change. This difficulty with the identification of lenders exists today under the guidance in Subtopic 470-50 for determining whether a debt modification is considered to be an extinguishment. Finally, the Board observed that if post-balance-sheet events are considered in relation to subsequent refinances of debt, the Board also would need to consider other post-balance-sheet events (for example, subsequent prepayments of debt).

Disclosures

BC31. In relation to classification of debt as a current liability or a noncurrent liability, one of the most useful disclosures consists of events affecting classification that occur between the balance sheet date and the financial statement issuance date. That is because that information assists resource providers in assessing the prospects for net cash inflows to (or outflows from) the reporting entity. Because the amendments in this proposed Update would prohibit such subsequent events from affecting the classification of debt as a current liability or a noncurrent liability (with the exception of debt covenant waivers), those disclosures would now be the primary source of that information in the financial statements. The Board observed that paragraph 855-10-50-2 currently requires disclosures related to subsequent events. For nonrecognized subsequent events, that guidance requires the disclosures of (a) the nature of the event and (b) an estimate of the event's financial effect, or a statement that such an estimate cannot be made.

BC32. The Board observed that there are limited disclosure requirements in GAAP related to the classification of debt other than the requirements related to subsequent events. The amendments in this proposed Update would replace existing disclosure requirements (that are primarily related to subjective acceleration clauses) with more comprehensive disclosure requirements about defaults. The Board determined that these disclosures would provide relevant information to users of financial statements for events that occurred as of the balance sheet date.

Effective Date and Transition

BC33. The Board decided that the amendments in this proposed Update would be applied prospectively in the first set of financial statements following the effective date. Although retrospective application would increase comparability with prior years, the Board concluded that the benefits of retrospective application would not justify the related costs. An entity would apply the proposed amendments to all debt arrangements, liability-classified mandatorily redeemable financial instruments within the scope of Subtopic 480-10, and debt with conversion and other options that are within the scope of Subtopic 470-20 that exist as of the effective date. The Board concluded that prospective application would provide financial statement users with the information needed in a cost-effective manner through the mix of information provided in the balance sheet and notes.

BC34. The effective date will be determined after the Board considers all stakeholder feedback on the amendments in this proposed Update. The Board decided to permit early adoption of the proposed amendments.

Amendments to the XBRL Taxonomy

The provisions of this Exposure Draft, if finalized as proposed, would require changes to the U.S. GAAP Financial Reporting Taxonomy (Taxonomy). We welcome comments on these proposed changes to the Taxonomy through ASU Taxonomy Changes provided at www.fasb.org. After the FASB has completed its deliberations and issued a final Accounting Standards Update, proposed amendments to the Taxonomy will be made available for public comment at www.fasb.org and finalized as part of the annual release process.