FINANCIAL ACCOUNTING STANDARDS BOARD

# Board Meeting Handout

# Codification Improvements to Financial Instruments

# January 29, 2020

## Meeting Purpose

1. The purpose of this decision-making Board meeting is to ask the Board for permission to draft a final Accounting Standards Update, *Codification Improvements to Financial Instruments*, for vote by written ballot. In November 2019, the Board issued a proposed Accounting Standards Update, *Codification Improvements,* that included eight issues related to the accounting for financial instruments. The staff believes that certain issues should be finalized separately from the broader Codification Improvements project to increase stakeholders' awareness of the amendments and to expedite the improvement process. In particular, some of the issues amend the guidance in Topic 326, Financial Instruments—Credit Losses, which is effective for public business entities, excluding smaller reporting companies as defined by the Securities and Exchange Commission, beginning in 2020. The staff would like to note that we have not included Issue 37 (Premium Amortization for Purchased Callable Debt Securities) in the Board meeting handout, which is from the proposed Update. Respondents provided substantive comments on this issue regarding the effective date of the proposed amendments that the staff will address at a future date.

2. The Board also will discuss the transition and effective date requirements, the cost-benefit analysis, and permission to proceed with the issuance of a final Update.

| Questions for the Board |
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| 1. Does the Board want to finalize the seven financial instrument related amendments listed in today's Board handout separately from the larger Codification Improvements project?<br><br>2. Does the Board affirm its previous decisions for the following amendments in the proposed Update:<br>a. Issue 1: Fair Value Option Disclosures (Issue 44 in the proposed Update)<br>b. Issue 2: Applicability of Portfolio Exception in Topic 820 to Nonfinancial Items (Issue 42 in the proposed Update)<br>c. Issue 3: Disclosures for Depository and Lending Institutions (Issue 50 in the proposed Update) |

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

d. Issue 4: Cross-Reference to Line-of-Credit or Revolving Debt Arrangements Guidance in Subtopic 470-50 (Issue 40 in the proposed Update)

e. Issue 5: Cross-Reference to Net Asset Value Practical Expedient in Subtopic 820-10 (Issue 43 in the proposed Update)

f. Issue 6: Interaction of Topic 842 and Topic 326 (Issue 38 in the proposed Update)

g. Issue 7: Interaction of Topic 326 and Subtopic 860-20 (Issue 49 in the proposed Update)?

3. Does the Board affirm its previous decisions regarding the effective date and transition requirements for Issue 1 through Issue 7?

4. Has the Board received sufficient information and analysis to make an informed decision on the perceived costs of the changes? If not, what other information or analysis is needed?

5. Does the Board think that the expected benefits justify the expected costs, thereby authorizing the staff to draft a final Accounting Standards Update for vote by written ballot?

## Comment Letter Feedback

3. The Board issued the proposed Update on November 26, 2019, and received 10 comment letters during the comment letter period, which ended on December 26, 2019. The following table provides information on the composition of comment letter respondents:

| Type of Respondent | Number of Respondents |
|---|---|
| **Preparers** | 0 |
| **Public Accounting Firms** | 7 |
| **State Societies of CPAs** | 2 |
| **Practitioner** | 1 |
| **Total Respondents** | **10** |

4. Overall, comment letter respondents supported most of the Board's amendments in this proposed Update related to the issues included in Question 2 to improve the accounting for various types of financial instruments. Respondents generally noted that the proposed amendments provide clarifications and improvements that will simplify or reduce operational concerns relating to the implementation of the recently issued standards.

5. The staff notes that comment letter respondents supported, and had no substantive comments on, the amendments in this proposed Update related to Issue 2 and Issue 5 included in Question 2. Therefore, those issues are not discussed in further detail below.

## Issue 1: Fair Value Option Disclosures

6. The amendments in this proposed Update would clarify that nonpublic entities are subject to the fair value option disclosures in paragraphs 825-10-50-24 through 50-32.

7. Comment letter respondents generally supported the amendments in this proposed Update. Two respondents noted that the proposed amendments may affect current practice and that the Board should provide entities with additional time to implement the proposed changes. Those respondents noted that additional time would allow private entities to learn about the changes through the annual continuing education cycle and to change systems, processes, and controls, as needed. One of the respondents noted that a one-year transition to make those changes would be helpful.

## Issue 3: Disclosures for Depository and Lending Institutions

8. The amendments in this proposed Update would clarify that for depository and lending institutions within the scope of Topic 942, the disclosure requirements in paragraphs 320-10-50-3, 320-10-50-5, and 320-10-50-5B apply to the disclosure requirements in paragraph 942-320-50-3. In particular, the guidance related to the disclosure of securities not due at a single maturity date in paragraphs 320-10-50-3, 320-10-50-5, and 320-10-50-5B also should apply to paragraph 942-320-50-3.

9. Comment letter respondents generally supported the amendments in this proposed Update. One respondent noted that the proposed amendments would be effective on January 1, 2020, for certain reporting entities and requested that the effective dates be extended because a final Update would not be issued before January 1, 2020.

## Issue 4: Cross-Reference to Line-of-Credit or Revolving Debt Arrangements Guidance in Subtopic 470-50

10. The amendments in this proposed Update would clarify that paragraph 470-50-40-18, which describes the accounting for third-party costs directly related to exchanges or modifications of debt instruments, references paragraph 470-50-40-21 for the accounting for modifications to or exchanges of line-of-credit or revolving-debt arrangements.

11. Comment letter respondents generally supported the amendments in this proposed Update. Two respondents noted that a similar amendment should be made to paragraph 470-50-40-17 related to fees between the debtor and creditor.

## Issue 6: Interaction of Topic 842 and Topic 326

12. The amendments in this proposed Update would align the contractual term to measure expected credit losses for a net investment in a lease under Topic 326 to be consistent with the lease term determined under Topic 842.

13. Comment letter respondents generally supported the amendments in this proposed Update. One respondent noted that the term *net investment in leases* is unclear on whether that term is referring to the defined term in Topic 842, and, if so, it should be referenced to the defined term. This respondent questioned whether the proposed amendments also would apply to leases acquired in a business combination and, therefore, should reference Topic 805.

14. One respondent noted that the amendments in this proposed Update could result in substantive changes to the application of the existing guidance requiring transition provisions. This respondent noted that additional feedback from reporting entities should be beneficial in determining the extent to which the proposed amendments would result in substantive changes to practice.

## Issue 7: Interaction of Topic 326 and Subtopic 860-20

15. The amendments in this proposed Update would clarify that when an entity regains control of financial assets previously sold, an allowance for credit losses should be recorded in accordance with Topic 326.

16. Comment letter respondents generally supported the amendments in this proposed Update. Three respondents noted that Topic 860 also provides initial measurement guidance (in addition to Topic 310, Topic 320, Topic 323, and Topic 325) for certain financial assets and recommended that the Board reference Topic 860 in the proposed guidance.

17. Two respondents noted that the transition guidance would require certain entities that have not yet adopted Accounting Standards Update No. 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Statements*, to adopt the amendments in this proposed Update as of January 1, 2020. Those respondents noted that the final guidance would not be issued before January 1, 2020, and, therefore, the effective date should be extended.

## Other Comments

18. One respondent noted that "there are ongoing discussions related to the measurement of an acquired net investment in a lease. Therefore, to the extent these discussions conclude that a different discount rate should be used, we believe the guidance should clarify whether the

discount rate used to measure credit losses on the net investment in a lease depends on whether the lease was originated or acquired."

19. One respondent noted the following:

> Changes should be made to [paragraph] 825-10-25-4 and the [Codification] master glossary definition of "remeasurement event" to reflect changes made to the Codification upon the issuance of [Subtopic] 2016-13. . . .. On the basis of our review of the amendments of [Subtopic] 2016-13, we believe that the removal of the language concerning an "other-than-temporary impairment" from [paragraph] 825-10-25-4 could create unintended consequences regarding whether the recognition of an other-than-temporary impairment of an equity method investment creates a remeasurement event that would allow an entity to elect the fair value option upon recognition of the impairment. We do not believe that the intent of [Subtopic] 2016-13 was to allow for this change in GAAP.