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Goodbye TDRs, hello loan mods and vintage disclosures: FAQ

By Sydney Garmong, Mandi Simpson, Alexis Ferry, and Steven King

A note from the authors

The Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2022-02, "Financial Instruments – Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures," in response to stakeholder feedback received during post-implementation review of the credit losses standard. This ASU eliminates troubled debt restructuring (TDR) accounting and the related disclosures, introduces new disclosure requirements for certain loan modifications, and modifies the vintage disclosure requirements to require disclosure of gross write-offs by year of origination. The ASU became effective for fiscal years beginning after Dec. 15, 2022, including interim periods.

As entities disclosed activity under this new ASU in the first quarter of 2023, questions about the scope of loan modifications requiring disclosure and how to address legacy TDRs arose frequently from financial statement users and preparers, particularly financial institutions.

The following answers have been prepared in response to questions accumulated during Crowe webinars, training sessions, and other events. The answers reflect our understanding of current accounting for loan modifications based on industry observations.

One common misconception is that TDRs are gone and no further activity is necessary. While ASU 2022-02 eliminates TDRs as we know them today, it is important to note that new disclosures are required under the standard for certain loan modifications. Essentially, the TDR process is replaced with another process to capture certain modifications for disclosures. Institutions should not underestimate the complexity of the process for complying with the new disclosure requirements. Compliance will require internal education on the provisions of the ASU along with refined internal processes and controls to ensure that the new disclosures are complete and accurate.

We hope that you find this information useful.

Sincerely,

Sydney Garmong
Mandi Simpson
Alexis Ferry
Steven King

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Topic A: Scoping considerations

A-1: What modifications are within the scope of the new ASU?

In order for a modification to be in scope, both of these criteria must be met:

1. The borrower must be experiencing financial difficulty. (Note: The indicators from legacy GAAP did not change.)
2. The modification is in the form of 1) principal forgiveness, 2) an interest-rate reduction, 3) an other-than-insignificant payment delay, or 4) a term extension.

Other forms of modifications, such as covenant waivers, adding or removing collateral or guarantors, or any other modification, are not qualifying modifications for disclosure. The disclosures are applicable only when an institution grants a modification that is one of the four modification types listed in the standard.

Topic B: General disclosure questions

B-1: What are the general disclosure requirements?

The ASU has two primary disclosure requirements for loan modifications in scope. The first requirement is that an institution must disclose the amount of commitments, if any, to lend additional funds to the borrower as of the date of each balance sheet presented.[1]

The second requirement is disclosure of certain quantitative and qualitative information about modifications and information about defaulted loans that were modified in the prior 12 months for each period for which a statement of income is presented.[2]

Crowe observation: For institutions with interim reporting requirements, any modification to a borrower in financial distress that occurs in the current quarter will be reflected in both the quarter-to-date and year-to-date disclosures, while any qualifying modification attributable to a prior quarter will be reflected in the year-to-date disclosures only.

[1] ASC 310-10-50-36.

[2] ASC 310-10-50-42 and 44.

B-2: What must an institution disclose under ASC 310-10-50-42 through ASC 310-10-50-44?

According to the Accounting Standards Codification (ASC), an institution should disclose the following for qualifying modifications made to borrowers experiencing financial difficulty:

Excerpt from the FASB ASC*

ASC 310-10-50-42

For each period for which a statement of income is presented, an institution shall disclose the following information related to modifications of receivables that are in the form of principal forgiveness, an interest rate reduction, an other-than-insignificant payment delay, or a term extension (or a combination thereof) made to debtors experiencing financial difficulty during the reporting period:

a. By class of financing receivable, qualitative and quantitative information about:
    1. The types of modifications utilized by an institution, including the total period-end amortized cost basis of the modified receivables and the percentage of modifications of receivables made to debtors experiencing financial difficulty relative to the total period-end amortized cost basis of receivables in the class of financing receivable.
    2. The financial effect of the modification by type of modification, which shall provide information about the changes to the contractual terms as a result of the modification and shall include the incremental effect of principal forgiveness on the amortized cost basis of the modified receivables, as applicable, or the reduction in weighted-average interest rates (versus a range) for interest rate reductions.
    3. Receivable performance in the 12 months after a modification of a receivable made to a debtor experiencing financial difficulty.
b. By portfolio segment, qualitative information about how those modifications and the debtors' subsequent performance are factored into determining the allowance for credit losses.

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ASC 310-10-50-43

Receivables may be modified in more than one manner. An institution that modifies the same receivable in more than one manner shall provide disclosures sufficient for users to understand the different types of combinations of modifications provided to borrowers. For example, a receivable may be modified to provide both principal forgiveness and an interest rate reduction. In that case, an institution shall disclose the period-end amortized cost basis of that receivable in a separate category that reflects that a combination of modification types has been granted. If another receivable was modified to provide both an interest rate reduction and a term extension, the period-end amortized cost basis of that receivable shall be presented in a different category. Multiple separate combination categories may be necessary if significant. The same receivable's period-end amortized cost basis shall not be presented in multiple categories.

ASC 310-10-50-44

For each period for which a statement of income is presented, an institution shall disclose the following information about financing receivables that had a payment default during the period and had been modified in the form of principal forgiveness, an interest rate reduction, an other-than-insignificant payment delay, or a term extension (or a combination thereof) within the previous 12 months preceding the payment default when the debtor was experiencing financial difficulty at the time of the modification:

a. By class of financing receivable, qualitative and quantitative information about those defaulted financing receivables, including the following:
    1. The type of contractual change that the modification provided
    2. The amount of financing receivables that defaulted, including the period-end amortized cost basis for financing receivables that defaulted.
b. By portfolio segment, qualitative information about how those defaults are factored into determining the allowance for credit losses.

B-3: Are illustrative disclosures available?

The ASU includes illustrative disclosures in 310-10-55-12A, “Example 3: Disclosures for Debtors Experiencing Financial Difficulty.”

Another alternative is the Crowe publication “Example CECL Disclosures: Financial Institutions.” Following are specific ASU 2022-02 illustrations:

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts in thousands except per share data)

NOTE <> - LOANS AND ALLOWANCE FOR CREDIT LOSSES (Continued)

Occasionally, the Company modifies loans to borrowers in financial distress by providing [disclose type of modification that is applicable – principal forgiveness, term extension, an other-than-insignificant payment delay or interest rate reduction]. When principal forgiveness is provided, the amount of forgiveness is charged-off against the allowance for credit losses.

In some cases, the Company provides multiple types of concessions on one loan. Typically, one type of concession, such as a term extension, is granted initially. If the borrower continues to experience financial difficulty, another concession, such as principal forgiveness, may be granted. For the loans included in the “combination” columns below, multiple types of modifications have been made on the same loan within the current reporting period. The combination is at least two of the following: [adjust list as applicable - a term extension, principal forgiveness, an other-than-insignificant payment delay and/or an interest rate reduction].

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts in thousands except per share data)

NOTE <> - LOANS AND ALLOWANCE FOR CREDIT LOSSES (Continued)

The following table presents the amortized cost basis of loans at December 31, 2022 that were both experiencing financial difficulty and modified during the year ended December 31, 2022, by class and by type of modification. The percentage of the amortized cost basis of loans that were modified to borrowers in financial distress as compared to the amortized cost basis of each class of financing receivable is also presented below:

Dollars in Thousands	Principal Forgiveness	Payment Delay	Term Extension	Interest Rate Reduction	Combination Term Extension and Principal Forgiveness[26]:	Combination Term Extension Interest Rate Reduction[26]	Total Class of Financing Receivable
Commercial	$	$	$	$	$	$	%
Commercial real estate:							
Construction							
Other							
Consumer:							
Credit Card							
Other							
Auto:							
Auto – direct							
Auto – indirect							
Residential real estate:							
Nontraditional							
Other							
Total	$	$	$	$	$	$	%

NOTE <> - LOANS AND ALLOWANCE FOR CREDIT LOSSES (Continued)

The Company has committed to lend additional amounts totaling $_____ to the borrowers included in the previous table.

The Company closely monitors the performance of loans that are modified to borrowers experiencing financial difficulty to understand the effectiveness of its modification efforts. The following table presents the performance of such loans that have been modified in the last 12 months:

	30 – 59 Days Past Due	60 – 89 Days Past Due	Greater Than 89 Days Past Due	Total Past Due
December 31, 2022				
Commercial	$	$	$	$
Commercial real estate:				
Construction				
Other				
Consumer:				
Credit card				
Other				
Auto:				
Auto – direct				
Auto – indirect				
Residential:				
Nontraditional				
Other				
Total	$	$	$	$

The following table presents the financial effect of the loan modifications presented above to borrowers experiencing financial difficulty for the year ended December 31, 2022:

	Principal Forgiveness	Weighted-Average Interest Rate Reduction	Weighted-Average Term Extension
Commercial	$	%	<months/years>
Commercial real estate:			
Construction			
Other			
Consumer:			
Credit card			
Other			
Auto:			
Auto – direct			
Auto – indirect			
Residential real estate:			
Nontraditional			
Other			
Total	$	$	$

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts in thousands except per share data)

NOTE <> - LOANS AND ALLOWANCE FOR CREDIT LOSSES (Continued)

The following table presents the amortized cost basis of loans that had a payment default during the year ended December 31, 2022 and were modified in the twelve months prior to that default to borrowers experiencing financial difficulty.

	Principal Forgiveness	Payment Delay	Term Extension	Interest Rate Reduction
Commercial	$	$	$	$
Commercial real estate:				
Construction				
Other				
Consumer:				
Credit Card				
Other				
Auto:				
Auto – direct				
Auto – indirect				
Residential real estate:				
Nontraditional				
Other				
Total	$	$	$	$

Upon the Company's determination that a modified loan (or portion of a loan) has subsequently been deemed uncollectible, the loan (or a portion of the loan) is written off. Therefore, the amortized cost basis of the loan is reduced by the uncollectible amount and the allowance for credit losses is adjusted by the same amount. [ASC 310-10-50-44 indicates qualitative information should be disclosed, by portfolio segment, regarding how the defaults are factored into determining the allowance for credit losses].

B-4: How long after the initial modification will an institution need to continue to disclose information about a modification to a borrower experiencing financial difficulty?

An institution must disclose information about how a qualifying modification performs in the 12 months following the modification.[3] If no subsequent qualifying modifications are made to that receivable, it would not need to be included in the current period's performance disclosures after the one-year period had passed. This concept is illustrated in the following example.

> **Example:** Assume a calendar year-end reporting company modifies a loan to a borrower in financial distress in a qualifying modification on Jan. 1, 20X3. The performance of that loan will be disclosed in the current period disclosures of all interim and annual financial statements that cover income statement periods that include calendar year 20X3. In financial statements with income statement periods commencing on or after Jan. 1, 20X4, the loan will no longer be included in the current period performance disclosures of loans modified to borrowers in financial distress assuming no further qualifying modification was made to the borrower in the current reporting period.

Topic C: New loan or a continuation of an existing loan

C-1: How should an institution determine if a loan modification results in a new loan or a continuation of an existing loan?

A modification results in a new loan if the new terms are at least as favorable to the institution as the terms for comparable loans to other customers with similar collection risks that are not refinancing or restructuring a loan. This test is satisfied when both of the following are true:

1. The new loan's effective yield is at least equal to the effective yield of the original loan.
2. Modifications to the original loan are deemed more than minor.[4]

To assess if the modification is more than minor, the institution should compare the present value of cash flows under the new and old loans.[5] If the present value of the cash flows is at least 10% different, the modification is deemed to be more than minor and results in a new loan. If the difference is less than 10%, further evaluation of relevant facts and circumstances must be made to determine if the more-than-minor condition has been satisfied.

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[3] ASC 310-10-50-42(a)(3).

[4] ASC 310-20-35-9.

[5] ASC 470-50-40-12.

C-2: What are examples of facts and circumstances that might indicate that a modification is more than minor, even if the cash flows before and after the modification are less than 10% different?

Determination of whether a modification that does not meet the 10% test is more than minor requires significant judgment. Relevant factors that might affect the assessment of whether a modification is more than minor might include:

- The magnitude of changes in the principal balance, interest rate, payment terms, and maturity date when compared to the original terms
- Changes in the guarantors or collateral securing the loan
- The significance of underwriting performed prior to approving the modification
- The rationale for approving the modification

C-3: What discount rate should be used when performing the 10% test described in Question C-1?

The discount rate that should be used to calculate the present value of the cash flows is the effective interest rate of the loan prior to the modification.

C-4: Are the disclosures for loans modified to borrowers in financial distress required only for modifications that resulted in the loan being treated as the continuation of an existing loan?

No. The disclosures are required whether or not the modification results in a new loan. In other words, the decision to include or exclude a modification from the required disclosures is made independent of the determination of whether the modification resulted in a new loan or not.

C-5: Is an institution required to disclose whether the modifications of a receivable made to borrowers experiencing financial difficulty resulted in a new loan or a continuation of an existing loan?

No. While the guidance requires certain qualitative disclosures, it does not require institutions to disclose if the modification resulted in a new loan or a continuation of an existing loan.

Topic D: Applying the financial difficulty criteria

D-1: How is "financial difficulty" defined?

The guidance from legacy GAAP remains unchanged. Indicators of financial difficulty could include, but are not limited to, the following:

- The borrower is currently in default.
- The borrower is in bankruptcy.
- There is substantial doubt about the borrower's ability to continue as a going concern.
- Without a modification, the borrower will not be able to obtain similar financing from another institution or continue to make payments.[6]

Judgment will be required to determine if the borrower is experiencing financial difficulty.

D-2: Prior guidance required borrowers in certain bankruptcy scenarios to be considered troubled debt restructurings. Are borrowers that have been identified as operating under certain bankruptcy scenarios required to be identified as experiencing financial difficulty?

Financial difficulty is considered probable if the borrower has declared or is in the process of declaring bankruptcy.[7] To the extent that the institution makes a qualifying modification to a borrower in bankruptcy, the modification must be disclosed under ASU 2022-02.

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[6] ASC 310-10-50-45.

[7] ASC 310-10-50-45.

Topic E: General modification observations

E-1: Would an interest-rate modification that is granted as a result of market trends meet the requirement to be included in the disclosure?

The required disclosures are applicable only if the borrower is experiencing financial difficulty. If the borrower is not experiencing financial difficulty, the modification would not meet the scope to be disclosed.

In the example of an interest-rate modification made in response to changing market trends, the institution must consider if the rate change would be reflective of a market interest rate to a borrower with similar collection risks. A rate *not* reflective of a market interest rate to borrowers of similar collections risks could be indicative of financial difficulty.

E-2: How does the ASU define "insignificant" in determining if a payment delay modification is significant?

ASU 2022-02 retains the legacy criteria for evaluating the significance of a payment delay. The guidance indicates that the following factors, when considered together, might indicate that a payment delay is insignificant[8]:

- The amount of restructured payment subject to the delayed payment is insignificant relative to the unpaid principal balance or collateral value of the loan and will result in an insignificant shortfall in the amount due.
- The delay in timing of the restructured payment period is insignificant relative to any of the following:
  - The frequency of payments due
  - The loan's original contractual maturity date
  - The loan's original expected duration

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[8] ASC 310-10-50-46.

In addition to this guidance, ASU 2022-02 introduces a new requirement that an institution must consider the cumulative effects of all restructurings occurring within the prior 12-month period to assess if the delay in payment is significant.[9] For example, consider the following fact pattern:

> **Example:** Institution A granted a payment delay modification to a borrower experiencing financial difficulty on March 15, 20X3, and concluded that the payment delay was insignificant. Therefore, this modification is not subject to the disclosure requirements under ASU 2022-02.
>
> On Dec. 15, 20X3, Institution A granted the same borrower a payment delay modification. Institution A must consider the modification from March 15, 20X3, and Dec. 15, 20X3, cumulatively when evaluating the significance of the new payment delay.

An institution should consider examples 4, 5, and 6 in ASC 310-10-55-12B through 55-12K for illustrative examples of payment delay evaluations.

E-3: What should an institution consider when evaluating the significance of a term extension?

For borrowers experiencing financial difficulty, a term extension might be granted. A restructuring that results only in a delay in payment that is considered insignificant is not required to be disclosed.[10] An institution should consider the factors enumerated in Question E-2 to assess if the delay is insignificant.

E-4: How is the cumulative payment delay criteria applied in disclosures?

An institution must consider the cumulative effect of all restructurings occurring within the prior 12-month period to assess if the payment delay is significant. For example, an institution with a June 30, 20X3, interim reporting period would assess the cumulative criteria based on the period from July 1, 20X2, through June 30, 20X3. Cumulative payment delays on restructurings that originated from April 1, 20X3, through June 30, 20X3, will be disclosed on both a quarter-to-date and year-to-date basis. Cumulative payment delays on restructurings that originated between June 30, 20X2, and March 21, 20X3, will be disclosed only on a year-to-date basis.

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[9] ASC 310-10-50-47.

[10] ASC 310-10-55-12I.

E-5: Do renewals made to borrowers experiencing financial difficulty meet the requirements to be disclosed under ASU 2022-02?

A renewal should be evaluated as a potential loan modification requiring disclosure. By its nature, a renewal generally results in a term extension. An institution should determine if the renewal also resulted in any other qualifying modification (that is, principal forgiveness, an interest-rate reduction, or an other-than-insignificant payment delay). To the extent that the renewal resulted in one, or a combination, of these qualifying modifications and was granted to a borrower experiencing financial difficulty the modification would be subject to the ASU 2022-02 disclosure requirements.[11]

E-6: Does a loan placed on nonaccrual satisfy the definition of a loan modification under the new ASU?

A loan placed on nonaccrual in isolation does not satisfy the disclosure criteria. The nonaccrual status would be a strong indicator of a borrower in financial distress. If a nonaccrual loan was also modified by granting principal forgiveness, an interest-rate reduction, an other-than-insignificant payment delay, or a term extension, the loan likely would need to be disclosed under the ASU.

E-7: What is the difference between a term extension and an other-than-insignificant payment delay?

While not expressly defined in authoritative guidance, a term extension generally is interpreted as a modification made to the contractual maturity of a loan. A payment delay generally is interpreted to mean a change in the due date of contractual cash flows (that is, contractual principal and interest, principal only, or interest only). Refer to Question E-2 for the criteria necessary to evaluate the significance of a payment delay. While differences exist between a term extension and an other-than-insignificant payment delay, overlapping factors often apply broadly to both forms of modifications.

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[11] ASC 310-10-50-36.

E-8: What are the guidelines or thresholds for when an extension would qualify for disclosure?

ASU 2022-02 largely retains the criteria for extension qualification from legacy authoritative guidance. That is, short-term extensions generally do not qualify for disclosure. While GAAP does not expressly define a definitive short-term extension, such a period generally has been interpreted to mean a period of 90 days or less. However, all facts and circumstances must be evaluated to ascertain if even a short-term extension would qualify for disclosure as discussed in Question E-9.

E-9: If an existing loan with a principal balloon payment due at maturity made to a borrower experiencing financial difficulty has a maturity date modification, with all other terms remaining equal, would this be a qualifying modification under the new disclosure requirements?

The FASB addressed this fact pattern as an illustrative example.[12] As illustrated, all facts and circumstances must be evaluated carefully. A short-term modification generally would not be viewed to trigger disclosure. However, to the extent that the extension is not short-term or is short-term but the borrower intends to pay the loan off through liquidation of collateral for which there is a significant shortfall of the collateral value relative to the unpaid principal balance, such modifications likely would need to be disclosed.

E-10: How should an interest-only modification made to a borrower experiencing financial difficulty be captured in the new disclosures?

It depends. An institution should evaluate the interest-only modification in relation to the four qualifying modification types to ascertain if the agreement triggered one or more of the qualifying modifications.

> **Crowe observation:** Most interest-only arrangements likely would be considered other-than-insignificant payment delays.

[12] ASC 310-10-55-12E.

Topic F: Individual evaluation considerations for allowance for credit losses

F-1: Is there a requirement to individually estimate the allowance for credit losses on loans modified to borrowers experiencing financial difficulty?

No. Identification of individually evaluated or collateral-dependent loans remains unchanged after adopting ASU 2022-02. If a loan is considered to have similar risk characteristics as other loans, it should be evaluated on a collective, or pooled, basis. Regardless of initial measurement, when a loan is determined to have risk characteristics different from other loans within its pool, it should be individually evaluated.

Topic G: Vintage disclosures

G-1: Is a public business entity required to provide gross write-off information by vintage and class of financing receivable?

Yes. A public business entity is required to present gross write-off information for the current period, on a year-to-date basis, by origination year.[13] ASC 326-20-50-3 should be applied by class of financing receivable. Therefore, a public business entity should present gross write-offs by class of financing receivable.

G-2: Does ASU 2022-02 require that a public business entity present gross write-off on a year-to-date basis, quarter-to-date basis, or both? Is comparative disclosure required?

As noted in Question G-1, gross write-off presentation should be on a year-to-date basis. Therefore, a public business entity is not required to provide quarter-to-date information. Consequently, a public business entity is not required to present such information on a comparative basis.

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[13] ASC 326-20-50-6.

G-3: If a public business entity concludes that a current period modification to a borrower experiencing financial difficulty constitutes a new loan, what should the loan's origination date be for the purposes of the vintage disclosures?

If the current period modification constitutes a new loan, the loan should be presented as a current period origination for the purposes of the required vintage disclosures.

Topic H: Operational considerations

H-1: Should institutions still be completing a modifications checklist, similar to those completed for troubled debt restructurings?

Institutions should consider any internal control over financial reporting (ICFR) and operational implications resulting from adoption of ASU 2022-02. They should establish policies, procedures, and controls to ensure the completeness of loans identified for disclosure purposes and the appropriate determination of whether the modification results in a new loan.

Legacy processes and checklists used to evaluate and identify TDRs will need to be modified to consider new factors and capture new data.

Topic I: Transition guidance

I-1: In adopting ASU 2022-02, what is the difference between using the prospective approach and using the modified retrospective approach?

If an institution applies the transition guidance prospectively, the institution will continue to account for existing TDRs under the legacy TDR accounting model, which uses a discounted cash flow method to determine the allowance for credit loss.

If an institution elects the modified retrospective transition approach, the institution will apply the current expected credit losses model to existing TDR loans and record the difference as a cumulative adjustment to opening retained earnings.

I-2: For modified retrospective implementation, what is the impact on initial disclosures? Do disclosures include previously modified loans or only the modifications since the date of adoption?

For both prospective and modified retrospective adoption, modifications made prior to the date of adoption do not need to be disclosed in an institution's financial statements.[14]

I-3: Are comparative disclosures required for the first year of adoption?

No. ASU 2022-02 is applicable only to modifications made on or after the date of adoption. Modifications made in prior periods are not subject to disclosure requirements.

I-4: What happens to prior period troubled debt restructuring disclosures as a result of ASU 2022-02 adoption?

Institutions will no longer be required to disclose prior period legacy TDR disclosures in periodic filings.[15]

I-5: Will the call report instructions be updated to reflect the impact of ASU 2022-02?

According to the March 2023 supplemental call report instructions, the agencies plan to revise the call report forms and instructions to replace the current TDR terminology with updated language from ASU 2022-02.

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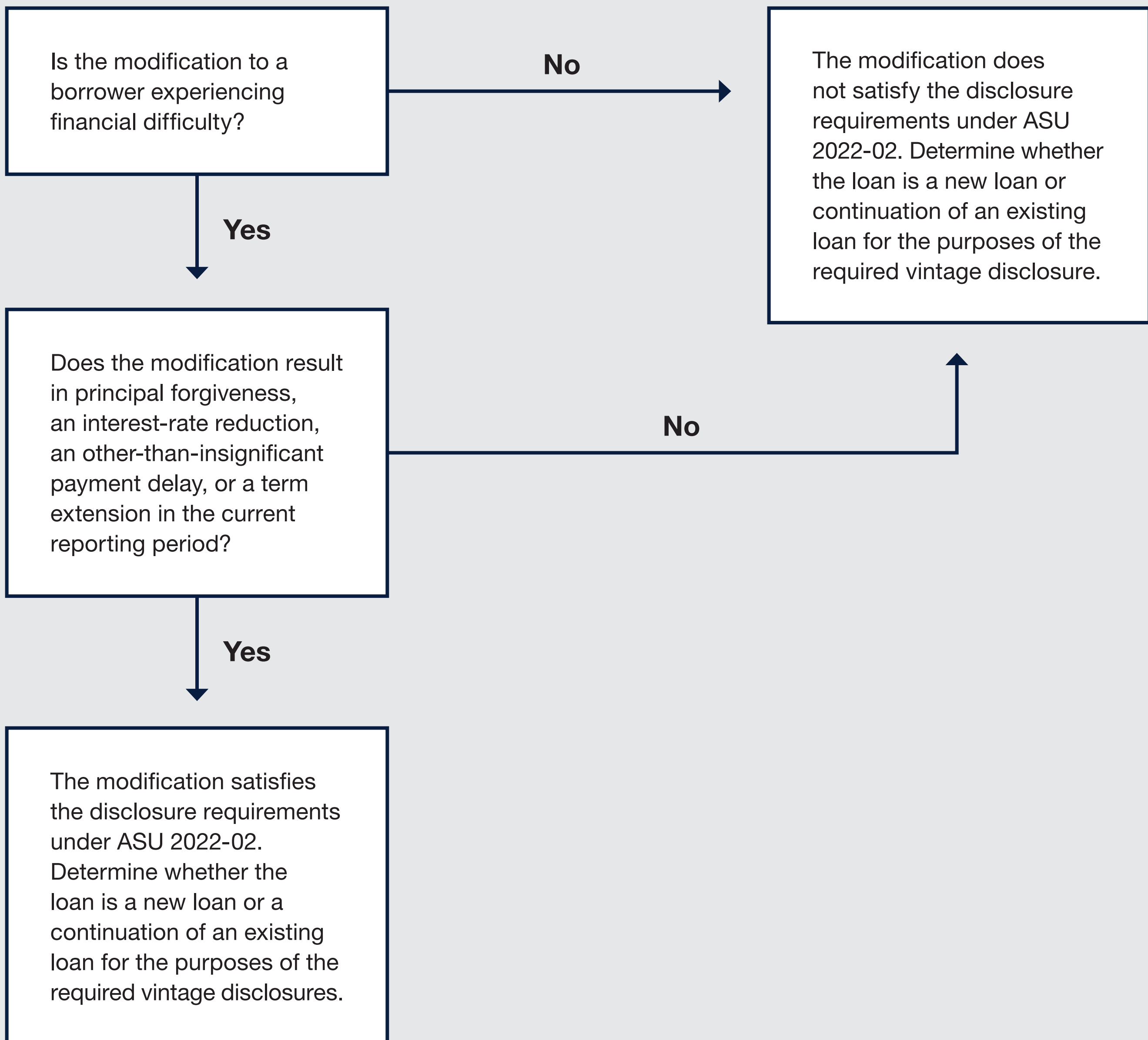
[14] ASC 326-10-65-5C(1).

[15] ASC 326-10-65-5.

Appendix A: Illustrative flowchart



Learn more

Sydney Garmong
Partner, National Office
+1 202 779 9911
sydney.garmong@crowe.com

Mandi Simpson
Partner, Accounting Advisory Leader
+1 404 442 1672
mandi.simpson@crowe.com

Alexis Ferry
+1 786 254 2428
alexis.ferry@crowe.com

Steven King
+1 859 280 5195
steven.king1@crowe.com

crowe.com

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