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TRG Snapshot
Meeting on Credit Losses

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Background

This *TRG Snapshot* summarizes the April 1, 2016, meeting of the FASB's transition resource group (TRG) for credit losses.

The purpose of the credit losses TRG is similar to that of the TRG that the FASB and IASB established to discuss their joint revenue recognition standard. That is, it does not issue guidance but provides feedback on potential implementation issues associated with the FASB's upcoming standard on accounting for credit losses. By analyzing and discussing such issues, the TRG helps the Board determine whether it needs to take additional action, such as providing clarification or issuing other guidance. The credit losses TRG comprises financial statement preparers, auditors, users, and financial services regulators. FASB members attend the TRG's meetings. In addition, representatives from the SEC, PCAOB, Federal Reserve, OCC,[1] FDIC,[2] NCUA,[3] and FHFA[4] are invited to observe the meetings.

Unlike the revenue recognition TRG, the credit losses TRG was created *before* the issuance of the final standard on credit losses to ascertain whether the guidance is understandable and to avoid potential implementation issues. The FASB will consider the TRG's feedback before finalizing the guidance on credit losses.

Editor's Note: The FASB spent much of 2015 drafting amendments to its impairment guidance. The amendments will introduce the current expected credit loss (CECL) model, which is a new impairment model for certain financial instruments that is based on expected losses rather than incurred losses. Under the CECL model, an entity would recognize as an allowance its estimate of credit losses that, when deducted from the amortized cost basis, would represent the "net amount expected to be collected on the financial asset." The FASB believes that the CECL model will result in more timely recognition of credit losses and will reduce the complexity of U.S. GAAP by decreasing the number of credit impairment models used to account for debt instruments. Under the existing impairment models (often referred to as incurred loss models), an impairment allowance is recognized only after a loss event (e.g., default) has occurred or its occurrence is probable. In assessing whether to recognize an impairment allowance, an entity may only consider current conditions and past events; it may not consider forward-looking information.

Topics Discussed at the Meeting

This was the credit losses TRG's first public meeting[5] with the FASB. At this meeting, the TRG discussed various aspects of the draft measurement guidance from the upcoming standard,[6] which will be

1 Office of the Comptroller of the Currency.
2 Federal Deposit Insurance Corporation.
3 National Credit Union Administration.
4 Federal Housing Finance Agency.
5 On September 30, 2015, the TRG held a private meeting to discuss an earlier draft of the credit losses standard.
6 The draft measurement guidance is available on the FASB's Web site.

codified in ASC 326-20, to ensure that the guidance is understandable and operational and reflects the Board's decisions to date. The discussion included the TRG's observations on how an entity would estimate expected credit losses on loans, specifically with respect to the draft measurement guidance stating that an entity:

- May use various methods to determine its expectation of credit losses.
- "[W]ill not be required to forecast conditions over the entire life of a financial asset."
- "[H]as flexibility to determine the historical loss information to which it would revert and the method of reversion."
- "[S]hould incorporate information [into] its expectations of credit losses that [is] relevant to the entity and accessible without undue cost or effort"; external information that is "less relevant than an entity's own internal information" would be excluded.

The TRG agreed that these concepts from the draft measurement guidance are clear.

Editor's Note: While the TRG believes that the measurement concepts discussed above are clearly articulated in the draft guidance, certain TRG members were concerned about what historical loss information an entity would revert to when estimating expected credit losses. Currently, the draft standard states that the entity would not be required to forecast conditions over the contractual life of the asset. Rather, for the period beyond the period for which the entity can make reasonable and supportable forecasts, the entity would revert to "historical credit loss experience."

While some Board members stated that an entity would have flexibility in choosing which historical loss information to revert to (e.g., unadjusted historical loss rates versus adjusted historical loss rates), others appeared not to support that view. Accordingly, some TRG members recommended that if the Board believes that an entity should have flexibility in choosing which loss experience to revert to, the draft should be revised to reflect that view. Alternatively, if the Board believes that an entity should always revert to an *unadjusted* historical loss amount as a practical way of putting the reversion concept into practice, the measurement guidance should be revised to articulate that view.

Next Steps

The FASB intends to meet at the end of April to (1) address certain TRG comments, (2) discuss whether the costs of implementing the standard would outweigh the benefits, and (3) decide whether to change the standard's effective date.[7] Further, the FASB staff will ask the Board for permission to finish drafting a final ASU for a vote by written ballot. The FASB believes that the standard will be issued by June 30, 2016.

[7] At its November 11, 2015, meeting, the FASB tentatively decided on an effective date for the upcoming standard. See Deloitte's November 12, 2015, journal entry for more information.

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