

New FASB Standard to Clarify TDR Recognition and Reporting

Overview: On April 5, 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update 2011-02 (ASU 2011-02), *A Creditor's Determination of Whether a Restructuring Is a Troubled Debt Restructuring*. FASB cited the need for additional guidance on the topic due to the current diversity in practice in identifying when the modification of a loan results in a troubled debt restructuring (TDR).

Key Changes: Although the definition of a TDR remains essentially unchanged, clarification of certain points may result in the identification of more TDRs than before the new guidance was applicable.

- **Financial Difficulty** – The new guidance requires creditors to consider the probability of payment default when determining whether a debtor is experiencing financial difficulty. In other words, even though a borrower is **not currently in default** on any if his or her debt, the borrower may be deemed to be experiencing financial difficulty if “it is **probable** that the debtor would be in payment default on any of its debt in the **foreseeable future** without the modification”.
- **Effective Interest Rate Test** – The new guidance explicitly precludes a creditor from applying the effective rate test (ASC 470) to determine whether a modification is a TDR.
- **Insignificant Delays in Payment** – A restructuring that results in an insignificant delay in payment is not a concession; however, the new guidance provides examples of various factors the creditor should consider in determining whether a delay in payment is insignificant.
- **Changes in Interest Rates** – A modification which results in a permanent or temporary increase in a loan’s contractual interest rate does not necessarily mean the modification is not a TDR because the new contractual interest rate on the restructured debt could still be below the market interest rate for new debt with similar characteristics.
- **Borrower’s Access to Funds** – The borrower’s inability to access funds at a market rate for debt with similar risk characteristics as the restructured debt would indicate the modification was executed at a below-market rate, which would likely indicate the creditor has granted a concession.

Effective Date: For public entities, this ASU is effective for the first interim or annual period beginning on or after June 15, 2011 and should be applied retrospectively to the beginning of the annual period of adoption. For nonpublic entities, this ASU is effective for annual periods ending on or after December 15, 2012, including interim periods within those annual periods.

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