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ASU 2015-03 and 2015-15: Simplifying the Presentation of Debt Issuance Costs and the Imputation of Interest

FOUR Q&AS THAT COVER EVERYTHING YOU NEED TO KNOW

In April 2015, the Financial Accounting Standards Board (FASB) released Accounting Standards Update (ASU) 2015-03 Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. It was issued as part of the FASB's Simplification Initiative, directed at identifying and improving generally accepted accounting principles (GAAP). Given the lack of clear authoritative guidance related to accounting for debt issuance costs associated with line-of-credit arrangement, the FASB issued ASU 2015-15 Interest - Imputation of Interest (Subtopic 835-30): Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements - Amendments to SEC Paragraphs Pursuant to Staff Announcement at June 18, 2015 EITF Meeting in August 2015.

So here's what you need to know about this new guidance:

Why were ASU 2015-03 and 2015-15 issued?

The FASB's objective of ASU 2015-03 is to reduce the complexity of having different balance sheet presentation requirements for debt issuance costs and debt discounts and premiums. In addition, ASU 2015-03 makes the reporting of debt issuance costs more aligned with International Financial Reporting Standards (IFRS) as well as FASB Concepts Statement Number 6, Elements of Financial Statements, which states that debt issuance costs cannot be an asset because they provide no future economic benefit.

ASU 2015-15 was issued by the FASB pursuant to the Securities and Exchange Commission (SEC) Staff Announcement at the June 18, 2015 Emerging Issues Task Force (EITF) meeting about the presentation and subsequent measurement of debt issuance costs associated with line-of-credit agreements. The guidance for the accounting for such costs was not addressed in the release of ASU 2015-03 and thus ASU 2015-15 was released to provide further clarification.

> There is significantly more information about your school's operations and management that board members can obtain from the audit and related financial statements if you know the right places to look and the right questions to ask.

What is the impact of ASU 2015-03 and 2015-15?

The resulting impact of ASU 2015-03 is that debt issuance costs shall be treated as a direct deduction from the carrying amount of the related debt (line-of-credit arrangements excluded), consistent with debt discounts. Amortization of debt issuance costs shall be reported as interest expense. This standard should be applied retroactively. As such, to comply with ASU 2015-03, comparative financial statements are required to be adjusted to conform to the new balance sheet presentation. This adjustment to the face of the financial statements consists of moving the debt issuance costs from assets to the liabilities section to offset the related debt. On the income statement the amortization of the debt issuance costs will be recorded as a component of interest expense.

In addition to the changes on the face of the financial statements, disclosures are required. A disclosure for a change in accounting principle is required in the period in which the change in presentation is made. Additionally, changes to the disclosure of debt and debt issuance costs are to be made to reflect the amount of borrowings outstanding as well as the unamortized debt issuance costs at each balance sheet date presented. Furthermore, the disclosure of the debt should reflect the effective interest rate on the borrowings net of the debt issuance costs, a change from the interest rate previously disclosed. The effective interest rate should be used in calculating the amortization of debt issuance costs as opposed to the straight-line method although this change may not be material.

The Private Company Counsel was opposed to this guidance and suggested that no change to the accounting for debt issuance costs be made or alternatively that debt issuance costs be expensed in the period incurred. The fear was that the presentation of debt net of debt issuance costs could be misleading to users of private company financial statements. The FASB discussed these alternatives but issued ASU 2015-03 in order to meet the objectives of the Simplification Initiative and comply with FASB Concepts Statement Number 6. Furthermore, the FASB felt that the disclosure of the debt and related debt issuance costs would provide users of the financial statements with relevant information about the borrowings.

Given the absence of authoritative guidance within ASU 2015-03 for debt issuance costs related to line-of-credit arrangements, the SEC stated it would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowing on the line-of-credit arrangements. The FASB did not make any changes to recognition or measurement of debt issuance costs as a part of this update.

When are ASU 2015-03 and 2015-15 effective?

For public business entities, ASU 2015-03 is effective for financial statements issued for fiscal years beginning after Dec. 15, 2015, and interim periods within those fiscal years.

For all other entities, ASU 2015-03 is effective for financial statements issued for fiscal years beginning after Dec. 15, 2015, and interim periods within fiscal years beginning after Dec. 15, 2016.

Although not required, early adoption of ASU 2015-03 is permitted. Entities who elect to adopt ASU 2015-03 early adoption will have the benefit of being in compliance with the most recent accounting pronouncements. In addition, it is recommended for all entities obtaining new debt so that the initial recording of debt issuance costs meets accounting standards that will be required for fiscal years beginning after December 15, 2015 ASU 2015-15 provides clarification for current accounting and effective immediately.

What do I need to do now?

Now is the time for entities, public and other, to begin discussions about ASU 2015-03 to determine the following:

1. When do we adopt the standard?
2. What will the new disclosures look like?
3. What is the effective interest rate of the debt net of the related debt issuance costs?
4. Should we modify the chart of accounts for ease of tracking outstanding borrowings and interest incurred on the note separate from amortization of debt issuance costs?
5. How do we account for debt issuance costs in a loan facility that includes both term debt and line-of-credit components?

Consulting with the users of your financial statements, management, internal and/or external auditors is a great place to start.

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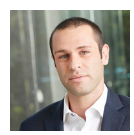

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