FASB Standard Simplifies Presentation of Debt Issuance Costs

On April 7, 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standard Update 2015-03 (ASU), *Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*. Debt issuance costs are those associated with issuing loans and bonds, such as fees and commissions paid to investment banks, law firms, auditors and regulators. Current U.S. generally accepted accounting principles (GAAP) require different presentation for debt discounts or premiums and debt issuance costs. Debt issuance costs are presented as a deferred asset, while any discounts or premiums are netted with the debt liability. This creates a conflict with Concepts Statement 6, *Elements of Financial Statements*, which defines an asset as having "future economic benefit."

The new guidance requires debt issuance costs to be presented as a direct deduction from the debt liability, consistent with debt discounts or premiums, rather than as a deferred asset. This is consistent with the guidance in Concepts Statement 6, which says debt issuance costs are similar to a debt discount and in effect reduce the proceeds of borrowing. Issuance costs would be reported as interest expense. Recognition and measurement guidance for debt issuance costs would not be affected by these amendments, which converge the treatment of debt issuance costs between U.S. GAAP and International Financial Reporting Standards (IFRS). The new presentation format also aligns with the Securities and Exchange Commission's accounting guidance for expenses related to equity offerings.

In its basis for conclusion, FASB acknowledges that costs may be incurred before an associated debt liability is recorded in the financial statements, e.g., *the costs are incurred before the proceeds are received or are related to an undrawn line of credit. However, FASB declined to provide explicit guidance in the ASU. The board observed that, in practice, entities defer issuance costs and apply them against the proceeds when received. Management's judgment will be required to address the presentation of debt issuance costs paid to secure revolving lines of credit when amounts are drawn and repaid periodically. It is not clear whether debt issuance costs associated with revolving lines of credit would be constantly reclassified between a contra-liability (outstanding balance) and an asset (zero balance). Judgment also will be required to allocate debt issuance costs to multiple debt instruments that are part of the same credit facility*

Presentation Example		
	December 31	
Note 1 – Long-Term Debt	20x2	20x1
Principal amount	$24,200,000	$24,200,000
Less unamortized discount and issue costs	2,680,000	2,792,000
Long-term debt less unamortized discount and issue costs	$21,520,000	$21,408,000
	Principal	Unamortized Discount & Issue Costs
6% subordinated debenture, due 20x9 (discount based on imputed interest rate of 7%)	$20,000,000	$2,150,000
6.5% bank loan, due 20x7	3,000,000	120,000
Noninterest bearing note issued in connection with acquisition of property, due 20x9 (discount based on imputed interest rate of 8%)	1,200,000	410,000
Total	**$24,200,000**	**$2,680,000**

Effective Date & Transition

The guidance would be adopted retrospectively. Upon transition, an entity would be required to comply with the applicable disclosures for a change in accounting principle, including the nature and reason for the change, a description of the prior-period information adjusted and the effect on the change in financial statement line items.

The guidance will be effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years, for public business entities. For all other entities, the guidance will be effective for annual periods beginning after December 15, 2015, and interim periods thereafter. For all entities, early adoption of the ASU is permitted for financial statements not previously issued.

For additional information, contact your BKD advisor.

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