AN ALERT FROM THE BDO NATIONAL ASSURANCE PRACTICE

# BDO FLASH REPORT
# FASB

## SUBJECT:

# FASB ISSUES ASU ON CLASSIFICATION OF CERTAIN GOVERNMENT-GUARANTEED MORTGAGE LOANS UPON FORECLOSURE

## SUMMARY:

The FASB recently issued ASU 2014-14[1] to address a practice issue related to the classification of certain foreclosed residential and nonresidential mortgage loans that are either fully or partially guaranteed under government programs. Specifically, creditors should reclassify loans that are within the scope of the ASU to “other receivables” upon foreclosure, rather than reclassifying them to other real estate owned (OREO). The ASU is available here.

## SCOPE, EFFECTIVE DATE AND TRANSITION:

ASU 2014-14 applies to all creditors that hold government-guaranteed mortgage loans, including those guaranteed by the U.S. Federal Housing Administration (FHA), the U.S. Department of Housing and Urban Development (HUD), and the U.S. Department of Veterans Affairs (VA).

The ASU is effective for public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. For all other entities, the amendments are effective for annual periods ending after December 15, 2015, and interim periods beginning after December 15, 2015.

An entity will adopt using either a prospective method or a modified retrospective method; however, it must apply the same transition method as elected under ASU 2014-04.[2] Application of the modified retrospective transition method will result in a cumulative-effect adjustment to reclassify affected balances to separate other receivables as of the beginning of the annual period of adoption. Early adoption is permitted, if the entity has already adopted ASU 2014-04.

[1] *Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure*
[2] *Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure*

## CONTACT:

**ADAM BROWN**
National Director of Accounting
214-665-0673 / abrown@bdo.com

**GAUTAM GOSWAMI**
National Assurance Partner
312-616-4631 / ggoswami@bdo.com

**CHRIS SMITH**
Audit & Accounting Professional Practice Leader
310-557-8549 / chsmith@bdo.com

## MAIN PROVISIONS:

Under the ASU, a creditor should derecognize a mortgage loan receivable and recognize a separate other receivable (distinct from loans) upon foreclosure when the following conditions are met.

a. The loan has a government guarantee that is not separable from the loan before foreclosure.

b. At the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover under that claim. A creditor would be considered to have the ability to recover under the guarantee at the time of foreclosure if the creditor determines that it has maintained compliance with the conditions and procedures required by the guarantee program.

c. At the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed.

The separate other receivable recorded upon foreclosure is to be measured based on the amount of the loan balance (principal and interest) the creditor expects to recover from the guarantor. Under the guidance in paragraph 310-40-40-6, foreclosure occurs when a creditor receives physical possession of real estate property collateralizing a mortgage loan.

In the basis for conclusions, the ASU indicates the new guidance should typically result in a balance-sheet only reclassification.