No. 2026-03
6 August 2026

Technical Line

FASB — final guidance

A closer look at FASB's amendments to expand the gross-up approach for purchased loans

In this issue:

What you need to know

- The FASB's amendments require entities to apply the gross-up approach in ASC 326 to all "purchased seasoned loans."
- Purchased seasoned loans are loans (excluding purchased financial assets with credit deterioration, credit card receivables, debt securities and trade receivables) that are either (1) acquired in a business combination or (2) obtained through a transfer that is not a business combination or initially recognized through the consolidation of a variable interest entity if certain seasoning criteria are met.
- A loan is considered seasoned if it is obtained more than 90 days after its origination date and the transferee was not involved in the origination.
- The amendments are effective for fiscal years beginning after 15 December 2026, including interim periods within those fiscal years. Entities are required to apply the guidance prospectively. Early adoption is permitted.

Overview

The Financial Accounting Standards Board (FASB or Board) **issued** a final Accounting Standards Update (ASU) expanding the use of the gross-up approach in Accounting Standards Codification (ASC) 326, *Credit Losses*, to all "purchased seasoned loans."

The ASU defines a purchased seasoned loan (PSL) as a loan[1] that is not a purchased credit deteriorated (PCD) financial asset, credit card receivable, debt security or trade receivable and that is either (1) acquired in a business combination or (2) obtained through a transfer that is not a business combination or initially recognized through the consolidation of a variable interest entity (VIE) if certain seasoning criteria are met. The guidance provides quantitative and qualitative criteria for determining when a non-PCD loan that is not acquired in a business combination is deemed seasoned.

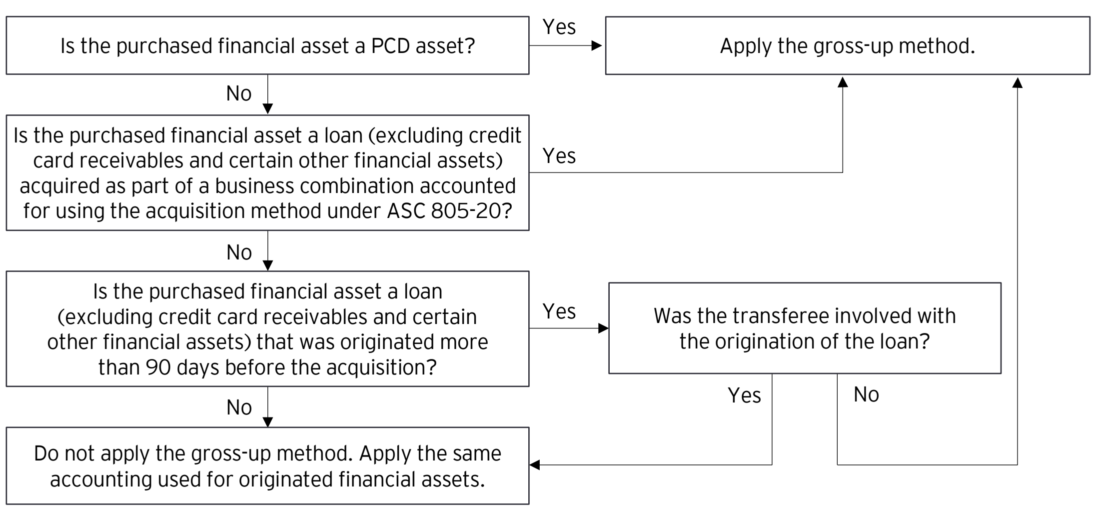
The amendments address concerns stakeholders raised during the FASB's post-implementation review of ASC 326 about the lack of comparability between PCD and non-PCD loans. Under current US GAAP, the gross-up approach is only applied to PCD assets (i.e., purchased financial assets that have experienced a more-than-insignificant deterioration in credit quality since origination). Judgment is needed in determining those assets that are PCD as "more-than-insignificant deterioration" is not defined in the guidance. Refer to section 5.2.1 of our Financial reporting developments publication, *Credit impairment under ASC 326*, for information on determining whether purchased financial assets are considered to be PCD.

Under the gross-up approach, an entity increases the initial amortized cost basis[2] of the acquired asset to include the asset's purchase price plus the initial estimate of expected credit losses. As a result, the allowance for credit losses at the acquisition date of the asset is recognized as an increase in the amortized cost basis of the acquired asset, rather than as a credit loss expense.

In contrast, the allowance for credit losses for non-PCD assets (i.e., acquired assets that have not experienced a more-than-insignificant credit deterioration since origination) is recorded separately through credit loss expense at the acquisition date. Because acquired financial assets are initially recognized at fair value (which already considers expected credit losses), this effectively resulted in a "double count" of the expected credit loss for non-PCD assets on their acquisition date and a Day 1 loss in the financial statements.

Stakeholders said the existence of different accounting approaches for PCD and non-PCD assets causes complexity and reduces comparability. They also noted that the Day 1 loss recorded for non-PCD assets is not intuitive and does not reflect the economics of the purchased assets. In response, the FASB amended ASC 326 to expand the population of purchased financial assets that would be accounted for under the gross-up approach.

The following decision tree shows when to account for a purchased financial asset using the gross-up approach under the new guidance:



Key amendments

Scope

The new guidance expands the use of the gross-up approach to the acquisition of non-PCD loans that are considered seasoned (i.e., PSLs). The ASU specifically excludes from the definition of PSLs credit card receivables, debt securities and trade receivables arising from transactions accounted for under ASC 606, *Revenue from Contracts with Customers*.

Loans are considered seasoned if they are either (1) acquired in a business combination accounted for under the acquisition method in ASU 805, *Business Combinations*, or (2) meet certain seasoning criteria if they are obtained through a transfer that is not a business combination or initially recognized through the consolidation of a VIE.

Non-PCD financial assets in the scope of ASC 326 that are not PSLs, such as debt securities and trade receivables, will continue to be accounted for by recording an allowance for credit losses through credit loss expense at their acquisition date.

How we see it

Entities are still required to determine whether purchased financial assets are PCD or non-PCD, since all PCD assets (not just loans) are subject to the gross-up approach. This determination also dictates whether an entity needs to consider the seasoning criteria in order to apply to the gross-up approach to the acquired loans.

Additionally, this determination is important because certain subsequent measurement and disclosure requirements apply only to PCD assets.

Question 1 Do the amendments apply to revolving credit arrangements that are not credit cards?

It depends. The Board decided to exclude non-PCD credit card receivables from the scope of the amendments in response to concerns about challenges in applying the gross-up approach to these assets because of the nature and volume of credit card transactions. However, the amended guidance does apply to the purchase of other non-PCD revolving credit arrangements.

These arrangements often have a funded and unfunded portion at the time of purchase. As such, entities would need to assess whether the loans acquired in these arrangements (i.e., the funded portion) represent PSLs. If so, they would be subject to the amendments.

While the unfunded portion is in the scope of ASC 326-20 if it is not unconditionally cancelable by the entity or accounted for as a derivative under ASC 815, this portion of the commitment is not subject to the amendments because it does not meet the definition of a loan. As such, a credit loss expense would be recorded for the unfunded portion upon acquisition of the arrangement. Any future draws after acquisition would be treated as originated loans.

Question 2 Do the amendments apply to forward purchase commitments to acquire non-PCD loans?

It depends. A forward commitment to purchase loans that are held for investment is in the scope of ASC 326-20 unless it is (1) unconditionally cancelable by the purchaser or (2) accounted for as a derivative in accordance with ASC 815.

While the amendments do not explicitly discuss forward purchase commitments, we believe it would be appropriate to apply the amendments to commitments that are in the scope of ASC 326-20 when the loans to be acquired under the commitment are considered PSLs as of the purchase commitment date. That is, we believe it would be appropriate for an entity not to record a credit loss expense at the inception of a commitment to purchase loans that are deemed to be PSL. This avoids a credit loss expense from being recorded at the commitment date that would otherwise be reversed upon acquisition of the loan. We understand this is generally consistent with practice for forward purchase commitments to purchase PCD loans in the scope of ASC 326-20. Refer to Question 4 for additional discussion on forward purchase commitments to acquire loans.

Question 3 Do the amendments apply to net investments in leases?

Net investments in leases are comprised of a financial component (i.e., a lease receivable) and a nonfinancial component (i.e., an unguaranteed residual asset). They are economically similar to loans, because the lease receivable component is considered a financing receivable that is a financial asset, and any unguaranteed residual asset component is usually not a significant portion of the net investment and is explicitly included in the scope of ASC 326-20.

Although the unguaranteed residual asset does not meet the definition of a financial asset, when issuing the guidance in ASC 326 and ASC 842, *Leases*, the Board decided that separately assessing the lease receivable under the ASC 326-20 expected credit loss impairment model and the unguaranteed residual asset under ASC 360, *Property, Plant, and Equipment*, would be overly complex with little benefit to financial statement users. Therefore, the Board concluded that the entire net investment in the lease should be measured for credit losses under ASC 326.

In contrast, the amendments do not specifically address whether the PSL guidance applies to a net investment in a lease. However, paragraphs BC19 and BC25 of the ASU's Background Information and Basis for Conclusions indicate that the Board considered including certain lease receivables in the scope of the guidance but decided to limit the scope of the amendments to loans.

The Board indicated that this focused approach would be responsive to stakeholder feedback about the unintuitive accounting for acquired loans without introducing additional complexity by requiring entities to evaluate the seasoning guidance for other financial assets in the scope of ASC 326 that did not materially contribute to stakeholders' concerns. As such, we believe it is reasonable to not apply the amended guidance to net investments in leases.

The seasoning guidance is intended to identify those purchased loans that are in-substance originations and account for them as originations at acquisition.

Seasoning criteria

The ASU limits the application of the gross-up approach to purchased non-PCD loans, excluding credit card receivables and certain other financial assets, that are deemed to be seasoned. The Board included the seasoning criteria to identify acquired financial assets that are economically similar to assets originated by the acquirer based on the substance of the transaction (i.e., financial assets that are effectively originated by a third party on behalf of the acquirer). The Board believes "non-seasoned" assets should be accounted for consistently with originated financial assets and not under the gross-up approach.

Loans acquired through a business combination accounted for using the acquisition method in accordance with ASC 805-20 are always considered seasoned and, therefore, are PSLs. Loans acquired in a transfer that is not a business combination (i.e., in an asset acquisition) or recognized through the consolidation of a VIE that is not a business are deemed to be seasoned if (1) they are acquired more than 90 days after origination (quantitative criterion) and (2) the transferee was not involved with their origination (qualitative criterion).

As discussed in ASC 326-20-30-17, the transferee is considered to be involved with the origination of the loan when either of the following occurs:

- The transferee has direct or indirect exposure to the economic risks and rewards of ownership within 90 days after the loan origination date.
- The transferee has substantive influence on the offering, arranging, underwriting or other nonadministrative lending activity performed by the originator (the transferor) related to the initial extension of credit to the debtor.

As stated by the Board in paragraph BC14 of the ASU's Basis for Conclusions, a transferee is more likely to be considered involved with the origination when contractual relationships exist between the transferee and the legal originator of the loan. Examples of such relationships include loss-sharing or make-whole arrangements where the purchaser is required to reimburse the originator for a loss of principal incurred before it acquires the loan or if the purchase transaction is terminated.

How we see it

The seasoning criteria include both a quantitative and qualitative element. While the 90-day quantitative threshold may be relatively simple to apply for many acquired loans, it may be more complex for revolving arrangements.

The qualitative assessment of an acquirer's involvement with the origination of loans purchased more than 90 days after origination will require judgment and consideration of all facts and circumstances.

Question 4 **How should the seasoning criteria be applied to forward purchase commitments to acquire non-PCD loans?**

It is common for entities to enter into purchase commitments to acquire loans at a future date. As discussed in Question 2, we believe it would be appropriate to apply the guidance in the ASU to forward purchase commitments that are in the scope of ASC 326-20 when the loans to be acquired under the commitment are considered to be PSLs as of the purchase commitment date.

Unless the purchase commitment is acquired through a business combination, the entity would need to determine whether the non-PCD loans to be acquired are seasoned based on the guidance in ASC 326-20-30-16 and 30-17. While this guidance does not specifically address commitments to purchase loans, we believe entities should consider whether the loans to be acquired are deemed seasoned as of the commitment date, as opposed to the purchase date. This view is based on the guidance in ASC 326-20-30-17(a), which indicates that a transferee is involved with the origination of a loan when it has direct or indirect exposure to the economic risks and rewards of ownership within 90 days after the loan origination date.

Because the transferee (i.e., the acquirer) is generally deemed to be exposed to the economic risk and rewards of the loans to be acquired under the purchase agreement as of the commitment date (assuming the terms of the purchase agreement, including the purchase price, are fixed as of this date), the loans to be acquired would need to have been originated at least 90 days before the commitment date to meet the qualitative seasoning criteria.

For example, if an entity enters into a three-month forward agreement to acquire a loan 30 days after the loan's origination, the loan would not meet the criteria to be deemed seasoned, even though the ultimate purchase of the loan would occur more than 90 days after its origination.

If the underlying loan meets the seasoning criterion in ASC 326-20-30-17(a), the acquiring entity would also need to consider the guidance in ASC 326-20-30-17(b) regarding whether it had substantive influence over the initial extension of credit to the debtor.

Question 5 How should the seasoning criteria be applied to the reacquisition of a loan by the originator?

The seasoning criterion in ASC 326-20-30-16(b)(2) requires that the transferee not be involved in the origination of the acquired loan. ASC 326-20-30-17 states that a transferee is involved with the loan's origination if either of the following occurs:

- The transferee has direct or indirect exposure to the economic risks and rewards of ownership within 90 days after the loan origination date.
- The transferee has substantive influence on the offering, arranging, underwriting or other nonadministrative lending activity performed by the originator (the transferor) related to the initial extension of credit to the debtor.

Based on this guidance, one might conclude that a loan reacquired by the originator would never qualify as a seasoned loan because the originator would always be deemed involved with its origination. However, we do not believe such a broad prohibition is consistent with the Board's intent given the statement in paragraph BC14 of the ASU's Basis for Conclusions that "[i]nvolvement with the origination of a loan is generally not considered relevant in the context of a subsequent reacquisition of a loan." Instead, the seasoning guidance appears intended to prevent a transferee from avoiding origination accounting and a Day 1 loss by acquiring a loan effectively originated by a third party on its behalf.

As such, we believe a loan that is reacquired more than 90 days after its origination date may be deemed seasoned if the intent of the sale and reacquisition of the loan is not deemed as a means to avoid origination accounting. Such a determination may require significant judgment.

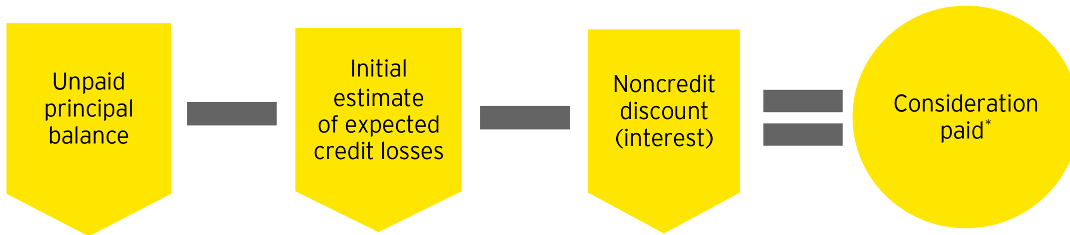
Accounting for purchased loans

Overview of the gross-up approach

Under current US GAAP, the gross-up approach is limited to the acquisition of PCD financial assets. Under this approach, an entity initially measures the amortized cost of a PCD asset by adding the acquisition date estimate of expected credit losses under the applicable impairment model to the asset's purchase price as illustrated below.

Under the gross-up approach, no credit loss expense is recognized upon acquisition because the initial allowance is established through the gross-up of the amortized cost. Distinguishing between the acquisition of PCD and non-PCD assets is important because an entity recognizes a credit loss expense on the income statement when it records the initial allowance for non-PCD assets.

Under the gross-up approach, any difference between the initial amortized cost (illustrated above) and the par value of a PCD asset represents the noncredit discount (or premium), which is amortized into interest income over the life of the asset.



* Purchase price or allocated fair value in a business combination, as applicable.

The guidance in ASC 326-20 does not require a specific method to be used to determine the initial estimate of expected credit losses at the date of acquisition. As such, the initial allowance for credit losses of PSL assets may be estimated using either a discounted cash flow (DCF) method or a non-DCF method.

An entity initially applies the same gross-up approach to PCD loans and PSLs, recognizing no credit loss expense for these loans at acquisition.

When an entity estimates credit losses for a PCD asset using a non-DCF method (e.g., an entity uses a loss-rate approach), the estimated credit losses are based on the unpaid principal balance (UPB) of the asset (i.e., the allowance for credit losses represents the amount of the UPB that is not expected to be collected). This differs from the allowance estimate under current US GAAP for a non-PCD asset, which is based on the asset's amortized cost basis.

An entity that uses a DCF approach to estimate credit losses for a PCD asset calculates the initial allowance for expected credit losses as the expected contractual cash shortfalls, discounted at the rate that equates the present value of estimated future cash flows with the financial asset's purchase price (i.e., the implied yield as of the purchase date).

After initial recognition, a PCD asset is generally accounted for under the credit loss model that applies to that type of asset. That is, an entity applies ASC 326-20 to credit losses on financing receivables, held-to-maturity debt securities and certain other instruments; ASC 326-30 to available-for-sale debt securities; and the guidance on other investments in ASC 325-40 to certain beneficial interests.

The ASU expands the use of the gross-up approach to PSLs in the scope of ASC 326-20 but does not change the accounting for PCD assets.

Recognition and initial measurement of purchased loans

The ASU requires an entity to apply the initial measurement guidance for PCD assets (described above) to PSLs. However, as discussed in paragraph BC29 of the ASU's Basis for Conclusions, the Board decided to tailor certain aspects of the subsequent measurement guidance under the gross-up approach for PSLs to reflect the fact that these assets have not experienced a more-than-insignificant deterioration in credit quality since origination. The amendments do not change the accounting for PCD assets, including PCD loans.

Under this approach, the initial allowance recognized is added to the purchase price (or fair value in a business combination) to arrive at the initial amortized cost basis. As a result, no credit loss expense is recognized upon the acquisition of these loans.

The following example illustrates an entity's initial accounting, before and after adopting the ASU, for a portfolio of loans (including PCD loans) that are purchased in a business combination.

Illustration 1 – Initial recognition of PCD loans and purchased seasoned loans

Company B is a calendar year-end entity that acquires a portfolio of loans with the following characteristics in a business combination accounted for using the acquisition method under ASC 805-20 as of 31 December 20X1:

- UPB of $100,000, of which $25,000 relates to loans that are PCD
- Fair value of $93,000, of which $20,000 relates to the PCD loans

Before adoption:

Company B uses a loss-rate approach and determines that the expected credit losses of the PCD loans as of the acquisition date are 16% of the UPB, or $4,000 [$25,000 x 16%]. The loss rate reflects past events, current conditions, and reasonable and supportable forecasts.

The PCD loans have an initial amortized cost basis on the acquisition date of $24,000 (the sum of the expected credit loss estimate of $4,000 and fair value of $20,000).

A separate valuation allowance for expected credit losses is recognized on the acquisition date, and no credit loss expense is recognized. Because the contractual amount due (UPB of $25,000) is more than the PCD loans' initial amortized cost ($24,000), a noncredit discount of $1,000 is also recognized.

The acquired non-PCD loans have an initial amortized cost basis equal to their purchase price of $73,000. Company C uses a loss-rate approach to determine that expected credit losses of the non-PCD loans are 2% of the amortized cost basis, or $1,460 [$73,000 x 2%]. The loss rate reflects past events, current conditions and reasonable and supportable forecasts.

An allowance for expected credit losses of $1,460 is recognized through credit loss expense. Because the contractual amount due ($75,000) is more than the non-PCD loans' purchase price ($73,000), a discount of $2,000 is also recognized.

The following journal entries are recorded on 31 December 20X1:[1]

Loans	$	25,000		
Loans (noncredit discount)			$	1,000
Allowance for credit losses				4,000
Cash				20,000

To account for the PCD loans at acquisition.

Loans	$	75,000		
Loans (discount)			$	2,000
Cash				73,000

To account for the non-PCD loans at acquisition.

Credit loss expense	$	1,460		
Allowance for credit losses			$	1,460

To recognize the allowance for credit losses on the non-PCD loans as of the reporting date.

After adoption:

Because the loans were acquired in a business combination, the non-PCD loans are all deemed to be seasoned and, therefore, are PSLs. Therefore, all of the purchased loans are accounted for on the acquisition date using the gross-up approach.

Company B uses a loss-rate approach and determines that the expected credit losses of the PCD loans as of the acquisition date are 16% of the UPB, or $4,000, and the expected credit losses of the PSLs are 2% of the UPB, or $1,500 [$75,000 x 25].[2] These loss rates reflect past events, current conditions and reasonable and supportable forecasts.

Company B determines that the PCD loans have an initial amortized cost basis on the acquisition date of $24,000 (the sum of the expected credit loss estimate of $4,000 and fair value of $20,000). Because the contractual amount due (UPB of $25,000) is more than the PCD loans' initial amortized cost ($24,000), a noncredit discount of $1,000 is also recognized on the acquisition date. The journal entry that is recorded on the acquisition of the PCD loans after adoption of the ASU is the same as the comparable entry recorded prior to adoption.

Additionally, as previously noted, because the non-PCD loans were acquired in a business combination, they are considered PSLs. Company B determines that the initial amortized cost basis of the PSLs on the acquisition date is $74,500 (the sum of the expected credit loss estimate of $1,500 and fair value of $73,000). Because the contractual amount due ($75,000) is more than the PSLs' initial amortized cost ($74,500), a noncredit discount of $500 is also recognized.

The following journal entries are recorded on 31 December 20X1:[1]

Loans	$	25,000		
Loans (noncredit discount)			$	1,000
Allowance for credit losses				4,000
Cash				20,000

To account for the PCD loans at acquisition.

Loans	$	75,000		
Loans (noncredit discount)			$	500
Allowance for credit losses				1,500
Cash				73,000

To account for the PSLs at acquisition.

1 For simplicity, the acquisition date and reporting date are the same in this illustration. When this is not the case, the allowance for credit losses for loans that apply the gross-up approach is recorded at acquisition through a gross-up of the loans' amortized cost, with no effect on earnings. On the reporting date following the acquisition, any change in estimated credit losses since the acquisition is recognized through credit loss expense.

2 For simplicity, this illustration assumes that the loss rate on the loans is the same before and after adoption of the ASU. However, in practice, the loss rate may differ.

The following example illustrates an entity's initial accounting, before and after adopting the ASU, for a portfolio of non-PCD loans (some of which are seasoned and some of which are not), that are purchased in an asset acquisition.

Illustration 2 – Initial recognition of non-PCD loans

Company C, a calendar year-end company, purchases a portfolio of loans with the following characteristics in an asset acquisition as of 31 December 20X1:

(1) UPB of $1,000,000, of which $900,000 relates to loans considered seasoned

(2) Purchase price of $1,100,000, of which $990,000 relates to loans considered seasoned

(3) None of the loans are deemed to be PCD

Before adoption:

Company C determines that the amortized cost basis of the purchased loans upon acquisition is equal to their purchase price of $1,100,000. Company C uses a loss-rate approach and determines that the expected credit losses of the purchased loans as of the acquisition date are 2% of the amortized cost basis, or $22,000 [$1,100,000 x 2%]. The loss rate reflects past events, current conditions and reasonable and supportable forecasts.

None of the loans are considered PCD, so an allowance for expected credit losses of $22,000 is recognized through credit loss expense (i.e., the gross-up approach is not applied). Because the purchase price ($1,100,000) is greater than the contractual amount due (UPB of $1,000,000), a premium of $100,000 is also recognized.

The following journal entries are recorded on 31 December 20X1:[1]

Loans	$ 1,000,000	
Loans (premium)	100,000	
Cash		$ 1,100,000

To account for the purchased loans at acquisition.

Credit loss expense	$ 22,000	
Allowance for credit losses		$ 22,000

To recognize the allowance for credit losses on the purchased loans on the reporting date.

After adoption:

Company C uses a loss-rate approach and determines that the expected credit losses as of the acquisition date for the loans deemed to be PSLs are 2% of the UPB, or $18,000 [$900,000 x 2%].[2] The loss rate reflects past events, current conditions and reasonable and supportable forecasts.

Company C determines that the initial amortized cost basis of the PSLs on the acquisition date is $ 1,008,000 (the sum of the expected credit loss estimate of $18,000 and purchase price of $990,000). A separate valuation allowance for expected credit losses is recognized on the acquisition date, and no credit loss expense is recognized. Because the initial amortized cost basis ($1,008,000) is greater than the contractual amount due (UPB of $900,000), a noncredit premium of $108,000 is also recognized on the acquisition date.

The amortized cost basis of the non-PSLs on acquisition is equal to their purchase price, or $110,000. Because the purchase price is greater than the contractual amount due (UPB of $100,000), a premium of $10,000 is recognized on the acquisition date.

Company C uses a loss-rate approach to determine that expected credit losses of the remaining purchased loans are 2% of the amortized cost basis, or $2,200 [$110,000 x 2%].[2] The loss rate reflects past events, current conditions, and reasonable and supportable forecasts.

An allowance for expected credit losses for the remaining loans is recognized through credit loss expense.

The following journal entries are recorded on 31 December 20X1:[1]

Loans	$	900,000		
Loans (noncredit premium)		108,000		
Allowance for credit losses			$	18,000
Cash				990,000
To account for the PSLs at acquisition.				
Loans	$	100,000		
Loans (premium)		10,000		
Cash			$	110,000
To account for the non-PSLs at acquisition.				
Credit loss expense	$	2,200		
Allowance for credit losses			$	2,200
To recognize the allowance for credit losses on the non-PSLs on the reporting date.				

[1] The acquisition date and reporting date are the same in this illustration, however, in practice they may differ. When this is the case, the allowance for credit losses for loans that apply the gross-up approach is recorded at acquisition through a gross-up of the loans' amortized cost, with no effect on earnings. On the reporting date following the acquisition, any change in estimated credit losses since the acquisition is recognized through credit loss expense.

[2] For simplicity, this illustration assumes that the loss rate on the loans is the same before and after adoption of the ASU. However, in practice, the loss rate may differ.

Allocating noncredit discounts or premiums to individual assets

When PCD assets or PSLs share similar characteristics under the expected credit loss model, an entity determines the amount of the initial allowance for credit losses at the group level. That amount represents the portion of the total discount at acquisition that relates to credit and is recognized as a gross-up of the purchase price to determine the group's amortized cost. Any difference between the UPB and the amortized cost is attributable to noncredit factors and results in a noncredit discount or premium.

The unit of account for recording the initial allowance for credit losses for a PCD asset or PSL is the individual asset. As such, when the initial allowance for a group of PCD assets or PSLs is determined at the group level, it needs to be allocated to each asset in the group for purposes of determining each individual asset's initial amortized cost. The allocation of the allowance for credit losses, along with the allocation of the purchase price, allows for the allocation of any noncredit discount or premium to each individual asset in the group, thus allowing for the calculation of each individual asset's effective interest rate (EIR).

An entity performs the following steps to allocate the noncredit discount or premium when the allowance for credit losses is determined on a collective (pool) basis:

Step 1	Allocate the purchase price to the individual assets
Step 2	Measure expected credit losses for the pool of assets
Step 3	Allocate the allowance for credit losses to each asset
Step 4	Add the allocated allowance from Step 3 to the allocated purchase price of each individual asset from Step 1 to arrive at each asset's amortized cost basis
Step 5	Determine the noncredit discount or premium for each asset, which is the difference between the asset's amortized cost basis from Step 4 and its UPB

In Step 1, the purchase price is allocated based on the fair value of each asset acquired in a business combination or their relative fair value when the sum of the individual fair values differs from the purchase price in an asset acquisition.

The guidance does not describe methods for allocating the allowance (Step 3). However, we believe a company should apply a method that is reasonable and rational based on the facts and circumstances. Examples of rational approaches may include a pro rata approach based on the individual assets' relative fair values or UPBs.

Subsequent measurement

The subsequent measurement guidance for PSLs is largely consistent with the gross-up approach currently applied to PCD loans. However, as mentioned above, the Board tailored certain aspects of the gross-up approach for PSLs to reflect the fact that these assets have not experienced a more-than-insignificant deterioration in credit quality since origination. These differences are discussed in the following subsections.

Interest accrual

The guidance on interest accrual for PSLs is consistent with that for PCD assets in the following ways:

- The discount related to credit losses embedded in the purchase price for a PSL is not recognized as interest income.[3]
- Any noncredit discount or premium associated with the acquisition of a PSL is required to be accreted into interest income over the life of the asset.

However, the accrual of interest may differ for PCD assets. ASC 310-10-35-53C states that for these assets the recognition of interest income depends on having a reasonable expectation about the amount expected to be collected. Because the ASU did not amend this guidance to include PSLs, entities will apply the same interest accrual policies for PSLs that they apply to their originated financial assets.

How we see it

While US GAAP does not specifically address nonaccrual policies for non-PCD loans, certain entities apply nonaccrual policies that are consistent with bank regulatory guidance. We believe entities that apply a nonaccrual policy should continue to do so consistently for their loans, including PSLs, after adopting the ASU. That is, adoption of the ASU would not change an entity's application of its nonaccrual policy.

While the subsequent measurement guidance for PSLs and PCD assets is largely consistent, there are certain differences because PSLs have not experienced a more-than-insignificant deterioration in credit quality since origination.

Recovery cap

Entities need to include expected recoveries of amounts they previously wrote off and expect to write off in their estimate of the allowance for credit losses, even if the recognition of these recoveries results in a negative allowance in accordance with ASC 326-20-30-13A.

However, for PCD assets, if an entity estimates expected credit losses using a method other than a DCF method, expected recoveries should not include any amounts that result in the accelerated recognition of the noncredit discount (i.e., the recovery cap). The amendments clarify that PSLs are not subject to the recovery cap guidance.

How we see it

ASC 326 requires a recovery cap for PCD assets to address concerns that an entity could accelerate the recognition of a non-credit discount by writing off the PCD asset and including the full principal amount as an estimated recovery (i.e., as a negative credit expense) in its estimate of expected credit losses.

However, because write-offs are expected to be less likely for PSLs than for PCD assets, the Board decided that PSLs should not be subject to the recovery cap. Instead, the recovery guidance PSLs is aligned with the guidance for originated loans.

This may result in different accounting outcomes for loans that become economically similar over time.

Measurement election

The amendments provide entities with the option to make an irrevocable election to subsequently measure the allowance for credit losses for PSLs using their amortized cost basis, instead of the unpaid principal balance typically required by the gross-up approach when the allowance for credit losses is estimated using a method other than a DCF method.

Entities would make this election on an acquisition-by-acquisition basis in the period of acquisition and apply it to all PSLs recognized in that acquisition. For example, if a calendar year-end company acquires loans on 31 January 2026, it would make the election in the period ending 31 March 2026 and apply it when estimating the allowance for credit losses reflected in the 31 March 2026 financial statements.

Because the election is made on an acquisition-by-acquisition basis, an entity that elects this option for one acquisition does not need to apply it to future acquisitions. For example, if two acquisitions occur in the same reporting period, an entity could make the election for one acquisition but not the other. An entity that elects this option should not remeasure the amortized cost basis or effective interest rate determined as of the acquisition date.

This election results in a change in the basis on which the allowance is calculated and, therefore, may result in an adjustment (i.e., one-time true-up) to the allowance for credit losses, which would be recognized in earnings in the period in which the acquisition occurs. The Board noted in paragraph BC31 of the ASU's Basis for Conclusions that it "expects that the amount of the true-up will be qualitatively and quantitatively insignificant, nonrecurring, and justified by the long-term benefit of collectively estimating expected credit losses."

How we see it

Allowing entities to subsequently measure the allowance for credit losses for PSLs using the amortized cost basis facilitates the pooling of PSLs with originated loans that share similar risk characteristics by aligning the basis used to estimate credit losses for both types of loans.

Disclosure requirements

The ASU requires entities to include the initial allowance for credit losses recognized on PSLs in the allowance rollforward (ASC 326-20-50-13) in interim and annual reporting periods. The amendments do not change the disclosure requirements for PCD assets.

While the ASU does not include explicit transition disclosure requirements, we believe it is appropriate for an entity adopting the ASU to make the applicable transition disclosures required under ASC 250, *Accounting Changes and Error Corrections*.

Effective date and transition

The amendments are effective for fiscal years beginning after 15 December 2026, including interim periods within those fiscal years. Early adoption is permitted.

An entity that adopts the guidance in an interim reporting period has the option to apply it as of the beginning of that interim period or the annual reporting period that includes that interim period. Entities are required to apply the amendments prospectively to PSLs acquired on or after the date of adoption.

Question 7 **Is a company that elects to early adopt the ASU in an interim period and apply the amendments as of the beginning of the annual reporting period required to adjust its previously issued interim financial statements for that annual period (if applicable)?**

No. The amendments require prospective adoption. For example, assume a calendar year-end company adopts the amendments in the second quarter of 20X1 and has already issued first-quarter financial statements reflecting a business combination that included a portfolio of non-credit card loans. If the entity elects to apply the amendments as of the beginning of 20X1, all loans acquired in that first-quarter business combination are considered seasoned as of the date of the acquisition.

The entity will reflect any adjustments related to applying the guidance effective 1 January 20X1 in its financial statements for the three and six months ended 30 June 20X1. The previously issued financial statements would not change.

Internal control considerations

The amended guidance may have implications for an entity’s internal control over financial reporting. Entities should evaluate whether they need to make changes to their existing processes and systems to capture the information required to determine whether acquired loans are PSLs and account for them under the new guidance.

The extent of an entity's experience with applying the gross-up approach under current US GAAP to PCD assets may impact the level of effort needed to apply the guidance. An entity that has limited experience with the gross-up approach (e.g., because they have not historically purchased financial assets deemed to be PCD) may need to implement new processes and controls to apply the gross-up approach to PSLs.

The ASU did not change the ASC 326-20 guidance on allocating the non-credit discount or premium to individual assets. However, entities that have not previously applied this guidance may need to put new processes and controls into place to allocate any non-credit discount or premium to the individual loans (e.g., entities that do not estimate expected credit losses using a DCF method).

Additionally, an entity's assessment of its level of involvement with the origination of loans purchased more than 90 days after origination (other than through a business combination) will require judgment.

For example, the facts and circumstances of a transaction, including any contractual relationships between the purchaser and the seller, will affect the determination of whether the entity was involved with the origination of the loan(s) purchased. The factors that management considers to determine its involvement with the origination of non-PCD purchased loans should be applied consistently, and the judgments made should be clearly documented.

Endnotes:

[1] The Master Glossary of the Codification defines a loan as "a contractual right to receive money on demand or on fixed or determinable dates that is recognized as an asset in the creditor's statement of financial position. Examples include but are not limited to accounts receivable (with terms exceeding one year) and notes receivable."

[2] The Master Glossary of the Codification defines the amortized cost basis as "the amount at which a financing receivable or investment is originated or acquired, adjusted for applicable accrued interest, accretion, or amortization of premium, discount, and net deferred fees or costs, collection of cash, write-offs, foreign exchange and fair value hedge accounting adjustments."

[3] The application of the gross-up approach results in an entity recognizing credit-related and (if applicable) non-credit related discounts at acquisition. However, only the latter is amortized into interest income. Excluding the initial credit-related discount can be viewed as effectively reducing interest income over the life of the loan.