Statement of Financial Accounting Standards No. 127

Note: This Statement has been completely superseded

FAS127 Status Page
FAS127 Summary

Deferral of the Effective Date of Certain Provisions of FASB Statement No. 125

an amendment of FASB Statement No. 125

December 1996

Financial Accounting Standards Board
of the Financial Accounting Foundation
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Statement of Financial Accounting Standards No. 127

Deferral of the Effective Date of Certain Provisions of FASB Statement No. 125

an amendment of FASB Statement No. 125

December 1996

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Paragraph Numbers

FAS 127: Deferral of the Effective Date of Certain Provisions of FASB Statement No. 125

an amendment of FASB Statement No. 125

FAS 127 Summary

FASB Statement No. 125, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* was issued in June 1996 and establishes, among other things, new criteria for determining whether a transfer of financial assets in exchange for cash or other consideration should be accounted for as a sale or as a pledge of collateral in a secured borrowing. Statement 125 also establishes new accounting requirements for pledged collateral. As issued, Statement 125 is effective for all transfers and servicing of financial assets and extinguishments of liabilities occurring after December 31, 1996.

The Board was made aware that the volume and variety of certain transactions and the related changes to information systems and accounting processes that are necessary to comply with the requirements of Statement 125 would make it extremely difficult, if not impossible, for some affected enterprises to apply the transfer and collateral provisions of Statement 125 to those transactions as soon as January 1, 1997. As a result, this Statement defers for one year the effective date (a) of paragraph 15 of Statement 125 and (b) for repurchase agreement, dollar-roll, securities lending, and similar transactions, of paragraphs 9-12 and 237(b) of Statement 125.

This Statement provides additional guidance on the types of transactions for which the effective date of Statement 125 has been deferred. It also requires that if it is not possible to determine whether a transfer occurring during calendar-year 1997 is part of a repurchase agreement, dollar-roll, securities lending, or similar transaction, then paragraphs 9-12 of Statement 125 should be applied to that transfer.

All provisions of Statement 125 should continue to be applied prospectively, and earlier or retroactive application is not permitted.

INTRODUCTION

1. FASB Statement No. 125, *Accounting for Transfers and Servicing of Financial Assets and*

Extinguishments of Liabilities, was issued in June 1996. That Statement establishes, among other things, new criteria for determining whether a transfer of financial assets should be accounted for as a sale or as a pledge of collateral in a secured borrowing. Statement 125 also establishes new accounting requirements for pledged collateral.

2. As issued, Statement 125 is effective for all transfers and servicing of financial assets and extinguishments of liabilities occurring after December 31, 1996, and is to be applied prospectively. Earlier or retroactive application of Statement 125 is not permitted.

3. The Board was made aware that the volume and variety of certain transactions and the related changes to information systems and accounting processes that are necessary to comply with the requirements of Statement 125 would make it extremely difficult, if not impossible, for some affected enterprises to apply the transfer and collateral provisions of Statement 125 to those transactions as soon as January 1, 1997. As a result, this Statement defers for one year the effective date (a) of paragraph 15 of Statement 125 and (b) for repurchase agreement, dollar-roll, securities lending, and similar transactions, of paragraphs 9-12 and 237(b) of Statement 125. The provisions of Statement 125 will continue to be applied prospectively, and earlier or retroactive application is not permitted.

4. To defer the effective date of paragraphs 9-12 and 237(b) of Statement 125 only for certain transactions, the Board has grouped all transfers of financial assets into two broad categories: (a) repurchase agreement, dollar-roll, securities lending, and similar transactions and (b) all other transfers and servicing of financial assets. As discussed in paragraph 14 of this Statement, the Board recognizes that it may be difficult to determine the appropriate categorization of certain transactions for purposes of determining the effective date of Statement 125 and therefore has provided guidance for those circumstances.

STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

Amendment to Statement 125

5. Paragraph 19 of Statement 125 is replaced by the following:

> This Statement shall be effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after December 31, 1996, except that:
>
> a. Paragraph 15 shall be effective for all transfers of financial assets occurring after December 31, 1997.
> b. For repurchase agreement, dollar-roll, securities lending, and similar transactions, paragraphs 9-12 and 237(b) shall be effective for transfers of financial assets occurring after December 31, 1997.

If it is not possible to determine whether a transfer occurring during calendar-year 1997 is covered by paragraph 19(b), then paragraphs 9-12 and 237(b) shall be applied to that transfer. All provisions of this Statement shall be applied prospectively, and earlier or retroactive application is not permitted.

Effective Date

6. This Statement is effective December 31, 1996.

The provisions of this Statement need not be applied to immaterial items.

This Statement was adopted by the unanimous vote of the seven members of the Financial Accounting Standards Board:

Dennis R. Beresford, *Chairman*
Joseph V. Anania
Anthony T. Cope
John M. Foster
Gaylen N. Larson
James J. Leisenring
Gerhard G. Mueller

Appendix: BACKGROUND INFORMATION AND BASIS FOR CONCLUSIONS

7. Statement 125 was issued in June 1996 and as issued is effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after December 31, 1996. As discussed in paragraph 229 of Statement 125, some respondents to the Exposure Draft had expressed concern about their ability to apply certain provisions of Statement 125 by that date, including making the changes to information and accounting systems needed to apply the newly established accounting requirements and efficiently track supporting data. The Board concluded that some of those concerns should be ameliorated by the effects of changes from the Exposure Draft and that in other cases data adequate for external financial reporting could be obtained in other ways while systems changes were being completed.

8. After Statement 125 was issued, however, representatives from various enterprises, particularly those representing brokers and dealers in securities, continued to express to the Board concerns about the effective date of Statement 125. On October 16, 1996, the Board met with representatives from interested enterprises to discuss those concerns, which focused on the

volume and variety of repurchase agreement, dollar-roll, securities lending, and similar transactions. The Board became convinced that, for those transactions, substantial changes to information systems and accounting processes were essential for brokers and dealers in securities and other enterprises to comply with Statement 125. The requisite changes and the volume and variety of those transactions would make it extremely difficult, if not impossible, for some affected enterprises to account for those transfers of financial assets and apply the secured borrowing and collateral provisions of Statement 125 as soon as January 1, 1997.

9. The Board appreciated the concerns expressed by those enterprises that attempting to account for those types of transactions manually until appropriate modifications could be made to information systems and accounting processes might lead to a significant temporary deterioration in the financial controls over and quality of financial information reported by the affected enterprises. Those enterprises informed the Board that a one-year delay for those transactions would provide an appropriate period of time for modifying information systems and accounting processes.

10. In November 1996, the Board issued an Exposure Draft, *Deferral of the Effective Date of Certain Provisions of FASB Statement No. 125,* that proposed deferring for one year the effective date of paragraph 15 (addressing secured borrowings and collateral) of Statement 125 for all transactions and of paragraphs 9-12 (addressing transfers of financial assets) only for transfers of financial assets that are part of repurchase agreement, dollar-roll, securities lending, and similar transactions. The Board did not believe that it was necessary or appropriate to defer the effective date of the other provisions of Statement 125 for other types of transactions because those provisions and transactions do not involve so great a volume or variety, nor do they involve such extensive changes to information systems and accounting processes. The Board received letters of comment from 29 respondents, a large majority of whom supported the Exposure Draft. The comments were considered by the Board during its redeliberations in a public meeting in December 1996, and the Board concluded that it could reach an informed decision on the basis of existing information without a public hearing.

11. The Board recognized that some enterprises that enter into repurchase agreement, dollar-roll, securities lending, and similar transactions and into collateral arrangements do so in volumes and varieties that would permit them to apply paragraphs 9-12 and 15 of Statement 125 to those transactions beginning on January 1, 1997, with little difficulty. However, the Board decided to require deferral rather than allow optional deferral because the Board continues to believe, for reasons discussed in paragraph 230 of Statement 125, that all parties should consistently apply Statement 125 to the same types of transactions and as of the same date.

12. To facilitate the deferral of the effective date of paragraphs 9-12 and 237(b) of Statement 125 for only the specified transactions, transfers of financial assets have been grouped into two broad categories. Transfers in the first category—repurchase agreement (refer to paragraphs 66-68 and 71 of Statement 125), dollar-roll (refer to paragraph 70 of Statement 125), securities lending (refer to paragraphs 61-64 of Statement 125), and similar transactions—frequently

involve an agreement that both entitles and obligates the transferor to repurchase or redeem the same or substantially the same (refer to paragraphs 27 and 28 of Statement 125) financial assets before their maturity. Other similar transactions include "buy-sell" agreements and certain other transfers of financial assets that are very similar to repurchase agreement, dollar-roll, and securities lending transactions in both form and objectives.

13. Transfers in the second category include securitizations (as defined in paragraph 243 of Statement 125) and other transfers of financial assets that, prior to the effective date of Statement 125, are accounted for in accordance with FASB Statements No. 77, *Reporting by Transferors for Transfers of Receivables with Recourse,* and No. 65, *Accounting for Certain Mortgage Banking Activities,* as amended by FASB Statement No. 122, *Accounting for Mortgage Servicing Rights,* and FASB Technical Bulletin No. 85-2, *Accounting for Collateralized Mortgage Obligations (CMOs)*. Transfers in the second category also include, but are not limited to, wash sales, loan syndications and participations, bankers' acceptances, and factoring arrangements (as discussed in Appendix A to Statement 125).

14. The Board recognized that in some cases it may be difficult to determine whether a transaction is better included in one category or the other for purposes of determining the effective date of Statement 125. As indicated in paragraph 5 of this Statement, if it is not possible to determine the category in which a transfer occurring during calendar-year 1997 should be included, then paragraphs 9-12 and 237(b) of Statement 125 should be applied to that transfer. That guidance is intended to be restrictive and does not allow an enterprise the option of including a transaction in one category or the other. The Board continues to believe that the effective date of Statement 125 should be the same for similar transactions, particularly for all parties to the same transaction.

Other Possibilities Considered

15. The Board considered not deferring any portion of Statement 125 for any type of transfer of financial assets. However, the Board concluded that that option would be unresponsive to a valid concern of some of its constituents. The Board then considered several possibilities for deferring the effective date of Statement 125. One possibility was deferring the effective date of the entire Statement for all transactions. Board members noted that that approach would be simpler. However, a number of constituents desire and have incurred significant effort and expense to apply the provisions of Statement 125 to securitizations, sales of mortgages and other receivables, and other transactions occurring after December 31, 1996. For that reason, the Board concluded that prohibiting those enterprises from applying the provisions associated with transfers and servicing of financial assets to those transactions as of the original effective date of Statement 125 would be undesirable.

16. The Board also considered permitting the choice of earlier or retroactive application. However, the Board continues to believe that, for the reasons discussed in paragraphs 230 and 231 of Statement 125, that would be undesirable.

17. The Board also considered deferring the effective date of Statement 125 with earlier implementation encouraged and requiring that the cumulative effect of applying Statement 125 to all transfers of financial assets and extinguishments of liabilities occurring after December 31, 1996 be recognized in the year beginning after December 15, 1997. The Board determined, however, that an approach that includes a cumulative-effect adjustment would not sufficiently alleviate the systems and administrative problems that the Board was attempting to respond to because it would continue to be necessary for affected enterprises to capture and process accounting information beginning with transfers occurring as soon as January 1, 1997.

18. The Board also considered deferring the effective date only for paragraph 15 of Statement 125. While that solution would perhaps be simpler than the other options that were considered and would address a portion of the problems raised by the affected enterprises, it would not address the information systems and accounting process requirements for a large volume and variety of transactions. Therefore, the Board concluded that deferring the effective date of only paragraph 15 was less desirable than the approach in this Statement.