Financial Accounting Standards Board

ORIGINAL PRONOUNCEMENTS

AS AMENDED

Statement of Financial Accounting Standards No. 166

Accounting for Transfers of Financial Assets

an amendment of FASB Statement No. 140

Statement of Financial Accounting Standards No. 166 Accounting for Transfers of Financial Assets

an amendment of FASB Statement No. 140

STATUS

Issued: June 2009

Effective Date: As of the beginning of each reporting entity's first annual reporting period beginning after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter

Affects: Amends FAS 140, paragraphs 2, 4 through 7, 9, 11, 12, 13, 13A, 14, 17, 27, 28, 29, 30, 32, 33, 47 through 49, 51, 53, 54, 55, 56 through 58, 60 through 65, 73 through 76, 78, 80 through 90, 92, 93, 97 through 100, 103, 104, 106, 112, 113, and 364 and footnotes 7 and 22
Adds FAS 140, paragraphs 7A through 7C, 8A, 8B, 10A, 11A, 16B through 16E, 26A through 26H, 27A, 27B, 29A, 46A, 54A, and 55A
Deletes FAS 140, paragraphs 8, 34 through 46, 59, 66, 67, 71, 72, 79, and 342 through 349A and footnotes 5a, 10, 15, 16, 17, and 33 through 36
Replaces FAS 140, paragraphs 10, 16A, 50, and 52 and footnotes 3, 6, 9, and 9a
Amends FAS 65, paragraph 6
Deletes FAS 155, paragraph 3
Amends FAS 156, paragraphs 2, 3(b), 3(d), and 3(g)
Deletes FAS 156, paragraphs 3(e) and 3(m)
Amends FAS 157, footnote 2
Deletes FIN 46(R), paragraphs 4(c) and 4(d) and footnote 27
Amends FTB 87-3, paragraph 9
Supersedes FSP FAS 140-2
Supersedes FSP FAS 140-4/FIN 46(R)-8

Affected by: No other pronouncements

Issues Discussed by FASB Emerging Issues Task Force (EITF)

Affects: Nullifies EITF Issue No. 02-12 and Topic No. D-66
Modifies EITF Issues No. 99-20 and 02-9 and Topic No. D-51

Interpreted by: No EITF Issues

Related Issues: EITF Issues No. 84-5, 84-20, 85-25, 85-40, 86-36, 87-18, 87-30, 88-20, 88-22, 89-2, 90-18, 92-2, 96-10, 96-19, 97-3, 98-8, 98-14, 98-15, and 99-8, and Topics No. D-65 and D-69

SUMMARY

Why Is the FASB Issuing This Statement and When Will It Be Effective?

The Board's objective in issuing this Statement is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets. The Board undertook this project to address (1) practices that have developed since the issuance of FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* that are not consistent with the original intent and key requirements of that Statement and (2) concerns of financial statement users that many of the financial assets (and related obligations) that have been derecognized should continue to be reported in the financial statements of transferors.

This Statement must be applied as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application is prohibited. This Statement must be applied to transfers occurring on or after the effective date.

Additionally, on and after the effective date, the concept of a qualifying special-purpose entity is no longer relevant for accounting purposes. Therefore, formerly qualifying special-purpose entities (as defined under previous accounting standards) should be evaluated for consolidation by reporting entities on and after the effective date in accordance with the applicable consolidation guidance. If the evaluation on the effective date results in consolidation, the reporting entity should apply the transition guidance provided in the pronouncement that requires consolidation.

Additionally, the disclosure provisions of this Statement should be applied to transfers that occurred both before and after the effective date of this Statement.

What Is the Scope of This Statement?

This Statement has the same scope as Statement 140. Accordingly, this Statement applies to all entities.

How Will This Statement Change Current Practice?

This Statement removes the concept of a qualifying special-purpose entity from Statement 140 and removes the exception from applying FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities,* to qualifying special-purpose entities.

This Statement clarifies that the objective of paragraph 9 of Statement 140 is to determine whether a transferor and all of the entities included in the transferor's financial statements being presented have surrendered control over transferred financial assets. That determination must consider the transferor's continuing involvements in the transferred financial asset, including all arrangements or agreements made contemporaneously with, or in contemplation of, the transfer, even if they were not entered into at the time of the transfer. This Statement modifies the financial-components approach used in Statement 140 and limits the circumstances in which a financial asset, or portion of a financial asset, should be derecognized when the transferor has not transferred the entire original financial asset to an entity that is not consolidated with the transferor in the financial statements being presented and/or when the transferor has continuing involvement with the transferred financial asset.

This Statement defines the term *participating interest* to establish specific conditions for reporting a transfer of a portion of a financial asset as a sale. If the transfer does not meet those conditions, a transferor should account for the transfer as a sale only if it transfers an entire financial asset or a group of entire financial assets and surrenders control over the entire transferred asset(s) in accordance with the conditions in paragraph 9 of Statement 140, as amended by this Statement.

The special provisions in Statement 140 and FASB Statement No. 65, *Accounting for Certain Mortgage Banking Activities,* for guaranteed mortgage securitizations are removed to require those securitizations to be treated the same as any other transfer of financial assets within the scope of Statement 140, as amended by this

Statement. If such a transfer does not meet the requirements for sale accounting, the securitized mortgage loans should continue to be classified as loans in the transferor's statement of financial position.

This Statement requires that a transferor recognize and initially measure at fair value all assets obtained (including a transferor's beneficial interest) and liabilities incurred as a result of a transfer of financial assets accounted for as a sale.

Enhanced disclosures are required to provide financial statement users with greater transparency about transfers of financial assets and a transferor's continuing involvement with transferred financial assets.

How Will This Statement Improve Financial Reporting?

This Statement improves financial reporting by eliminating (1) the exceptions for qualifying special-purpose entities from the consolidation guidance and (2) the exception that permitted sale accounting for certain mortgage securitizations when a transferor has not surrendered control over the transferred financial assets. In addition, comparability and consistency in accounting for transferred financial assets will be improved through clarifications of the requirements for isolation and limitations on portions of financial assets that are eligible for sale accounting.

This Statement enhances the information provided to financial statement users to provide greater transparency about transfers of financial assets and a transferor's continuing involvement, if any, with transferred financial assets. Under this Statement, many types of transferred financial assets that would have been derecognized previously are no longer eligible for derecognition. This Statement requires enhanced disclosures about the risks that a transferor continues to be exposed to because of its continuing involvement in transferred financial assets.

This Statement also clarifies and improves certain provisions in Statement 140 that have resulted in inconsistencies in the application of the principles on which that Statement is based.

What Is the Effect of This Statement on Convergence with International Financial Reporting Standards?

The International Accounting Standards Board (IASB) has projects on its agenda to develop new standards on derecognition and consolidation. The IASB issued two related Exposure Drafts—*Consolidated Financial Statements,* and *Derecognition*—in December 2008 and March 2009, respectively.

This Statement is designed to provide a short-term solution to address inconsistencies in practice in the context of the existing concepts in Statement 140. In the short term, this project improves convergence by eliminating the concept of a qualifying special-purpose entity, which does not exist in International Financial Reporting Standards, and by limiting the portions of financial assets that are eligible for derecognition. This project also incorporates certain of the disclosures currently required by IFRS 7, *Financial Instruments: Disclosures.* Ultimately, the two Boards will seek to issue a converged derecognition standard.

Statement of Financial Accounting Standards No. 166

Accounting for Transfers of Financial Assets

an amendment of FASB Statement No. 140

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OBJECTIVE

1. The objective of this Statement is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial reports about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement in transferred financial assets.

2. This Statement amends FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* as follows:

a. It removes the concept of a qualifying special-purpose entity from Statement 140 and removes the exception from applying FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities,* to variable interest entities that are qualifying special-purpose entities.
b. It modifies the financial-components approach used in Statement 140 and limits the circumstances in which a transferor derecognizes a portion or component of a financial asset when the transferor has not transferred the original financial asset to an entity that is not consolidated with the transferor in the financial statements being presented and/or when the transferor has continuing involvement with the financial asset.
c. It establishes the following conditions for reporting a transfer of a portion (or portions) of a financial asset as a sale:
    (1) The transferred portion (or portions) and any portion that continues to be held by the transferor must be participating interests as described in paragraph 8B of Statement 140, as amended by this Statement.
    (2) The transfer of the participating interest (or participating interests) must meet the conditions for surrender of control in paragraph 9 of Statement 140, as amended by this Statement.

    If the transfer does not meet these conditions, sale accounting can be achieved only by transferring an entire financial asset or group of entire financial assets in a transaction that meets the sale accounting conditions in paragraph 9 of Statement 140, as amended by this Statement.
d. It defines a participating interest as a portion of a financial asset that:
    (1) Conveys proportionate ownership rights with equal priority to each participating interest holder.

(2) Involves no recourse (other than standard representations and warranties) to, or subordination by, any participating interest holder.
(3) Does not entitle any participating interest holder to receive cash before any other participating interest holder.

e. It clarifies that an entity must consider all arrangements or agreements made contemporaneously with, or in contemplation of, a transfer, even if not entered into at the time of the transfer, when applying the conditions in paragraph 9 of Statement 140, as amended by this Statement. In addition, it explicitly clarifies that the application of the conditions in paragraph 9 must consider the transferor's continuing involvement with transferred financial assets.
f. It clarifies the isolation analysis to ensure that the financial asset has been put beyond the reach of the transferor, any of its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented, and its creditors.
g. It removes the exception in paragraph 9(b) for transfers to qualifying special-purpose entities. It requires that a transferor, in a transfer to an entity whose sole purpose is to engage in securitization or asset-backed financing activities, determine whether each third-party holder of a beneficial interest in that entity has the right to pledge or exchange its beneficial interest and that no condition both:
   (1) Constrains the third-party beneficial interest holder from taking advantage of its right to pledge or exchange; and
   (2) Provides more than a trivial benefit to the transferor.
h. It clarifies the principle in paragraph 9(c) that the transferor must evaluate whether it, its consolidated affiliates included in the financial statements being presented, or its agents effectively control the transferred financial asset directly or indirectly.
i. It requires that a transferor recognize and initially measure at fair value all assets obtained (including a transferor's beneficial interest) and liabilities incurred as a result of a transfer of an entire financial asset or a group of financial assets accounted for as a sale.
j. It removes the special provisions in Statement 140 and FASB Statement No. 65, *Accounting for Certain Mortgage Banking Activities,* for guaranteed mortgage securitizations to require them to be treated the same as any other transfer of financial assets within the scope of Statement 140, as amended by this Statement. If such a transfer does not meet the conditions for sale accounting, the securitized mortgage loans shall continue to be classified as loans.
k. It removes the fair value practicability exception from measuring the proceeds received by a transferor in a transfer that meets the conditions for sale accounting at fair value.
l. It requires enhanced disclosures to provide financial statement users with greater transparency about transfers of financial assets and a transferor's continuing involvement with transfers of financial assets accounted for as sales.

STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

Scope

3. This Statement has the same scope as Statement 140. Accordingly, this Statement applies to all entities.

Amendments to Statement 140

4. Statement 140 is amended as follows: [Added text is underlined and deleted text is ~~struck out~~.]

a. Paragraph 2:

   Transfers of financial assets take many forms. Accounting for transfers in which the **transferor** has no **continuing involvement** with the transferred financial assets or with the **transferee** has not been controversial. However, transfers of financial assets often occur in which the transferor has some continuing involvement either with the assets transferred or with the transferee. Examples of continuing involvement with the transferred financial assets include, but are not limited to, servicing arrangements, **recourse,** ~~servicing,~~ or guarantee arrangements, agreements to ~~reacquire~~ purchase or redeem transferred financial assets, options written or held, **derivative financial instruments** that are entered into contemporaneously with, or in contemplation of, the transfer, arrangements to provide financial support, ~~and~~ pledges of **collateral,** and the transferor's **beneficial interests** in the transferred financial assets. Transfers of financial assets with continuing involvement raise issues about the circumstances under which the transfers should be considered as sales of all or part of the assets or as secured borrowings and about how transferors and transferees should account for sales and secured borrowings. This Statement establishes standards for resolving those issues.

b. Paragraph 4, as amended:

This Statement does not address transfers of custody of financial assets for safekeeping, contributions,[2] transfers of ownership interests that are in substance sales of real estate, or investments by owners or distributions to owners of a business enterprise. This Statement does not address subsequent measurement of assets and liabilities, except for (a) **servicing assets** and **servicing liabilities** and (b) **interest-only strips,** ~~securities,~~ other beneficial interests ~~that continue to be held by a transferor in securitizations~~, loans, other receivables, or other financial assets that can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment and that are not within the scope of FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities.* This Statement does not change the accounting for employee benefits subject to the provisions of FASB Statement No. 87, *Employers' Accounting for Pensions,* No. 88, *Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits,* or No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions.* This Statement does not change the provisions relating to leveraged leases in FASB Statement No. 13, *Accounting for Leases,* or money-over-money and wrap lease transactions involving nonrecourse debt subject to the provisions of FASB Technical Bulletin No. 88-1, *Issues Relating to Accounting for Leases.* This Statement does not address transfers of nonfinancial assets, for example, servicing assets, or transfers of unrecognized financial assets, for example, minimum lease payments to be received under operating leases.

c. Paragraph 5, as amended:

The Board concluded that an objective in accounting for transfers of financial assets is for each entity that is a party to the transaction to recognize only assets it controls and liabilities it has incurred, to **derecognize** assets only when control has been surrendered, and to derecognize liabilities only when they have been extinguished. Sales and other transfers may ~~frequently~~ result in a disaggregation of financial assets and liabilities into components, which become separate assets and liabilities. ~~For example, if an entity sells a portion of a financial asset it owns, the portion that continues to be held by a transferor becomes an asset separate from the portion sold and from the assets obtained in exchange.~~

d. Paragraph 7:

Before FASB Statement No. 125, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* accounting standards generally required that a transferor account for financial assets transferred as an inseparable unit that had been either entirely sold or entirely retained. Those standards were difficult to apply and produced inconsistent and arbitrary results. For example, whether a transfer "purported to be a sale" was sufficient to determine whether the transfer was accounted for and reported as a sale of receivables under one accounting standard or as a secured borrowing under another. After studying many of the complex developments that have occurred in financial markets leading up to the issuance of Statement 125 ~~during recent years~~, the Board concluded that previous approaches that viewed each financial asset as an indivisible unit do not provide an appropriate basis for developing consistent and operational standards for dealing with transfers and servicing of financial assets and extinguishments of liabilities. To address those issues adequately and consistently, the Board decided to adopt as the basis for ~~this~~ Statements 125 and 140 a *financial-components approach* that focuses on control and recognizes that financial assets and liabilities can be divided into a variety of components.

e. Paragraphs 7A through 7C are added as follows:

7A. The Board received a number of requests after the issuance of Statement 125 to reconsider or clarify the conditions for sale accounting and to expand the disclosure requirements of that Statement. In response to those requests, the Board decided to replace Statement 125 with this Statement, even though the financial-components approach and many other provisions of Statement 125 were carried forward without reconsideration.

7B. However, after this Statement was issued, the Board received a number of requests from financial statement users and regulators to reconsider whether limits should be placed on the application of the financial-components approach to transfers of portions of a financial asset when the transferor also has significant continuing involvement with the transferred financial assets and continues to hold custody of the original financial assets. The Board continued to receive requests from financial statement users, regulators, preparers, and auditors to address other application issues. Other matters that the Board was asked to reconsider or clarify included:

a. The permitted activities of qualifying special-purpose entities
b. Isolation analysis
c. Effective control
d. The initial measurement of the transferor's interests in transferred financial assets
e. Disclosures.

7C. The Board decided to undertake a project to amend this Statement to address those concerns. The Board issued FASB Statement No. 166, *Accounting for Transfers of Financial Assets,* in June 2009 to amend this Statement. Statement 166 modifies the financial-components approach and also removes the concept of a qualifying special-purpose entity, clarifies the isolation and effective control conditions for sale accounting in paragraph 9, amends initial measurement of a transferor's interest in transferred financial assets, and requires additional disclosures. The Board also undertook a project to amend FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities,* due in part to the elimination of the qualifying special-purpose entity concept and the expectation that many **securitization** entities previously exempt from Interpretation 46(R) would become subject to its provisions. That project resulted in FASB Statement No. 167, *Amendments to FASB Interpretation No. 46(R),* which was issued together with Statement 166 in June 2009.

f. Paragraph 8:

~~The Board issued Statement 125 in June 1996. After the issuance of that Statement, several parties called for reconsideration or clarification of certain provisions. Matters the Board was asked to reconsider or clarify included:~~

~~a. Circumstances in which a special-purpose entity (SPE) can be considered qualifying~~
~~b. Circumstances in which the assets held by a qualifying SPE should appear in the consolidated financial statements of the transferor~~
~~c. Whether sale accounting is precluded if the transferor holds a right to repurchase transferred assets that is attached to, is embedded in, or is otherwise transferable with the financial assets~~
~~d. Circumstances in which sale accounting is precluded if transferred financial assets can be removed from an SPE by the transferor (for example, under a removal-of-accounts provision (ROAP))~~
~~e. Whether arrangements that obligate, but do not entitle, a transferor to repurchase or redeem transferred financial assets should affect the accounting for those transfers~~
~~f. The impact of the powers of the Federal Deposit Insurance Corporation (FDIC) on isolation of assets transferred by financial institutions~~
~~g. Whether transfers of financial assets measured using the equity method of accounting should continue to be included in the scope of Statement 125~~
~~h. Whether disclosures should be enhanced to provide more information about assumptions used to determine the fair value of retained interests and the gain or loss on financial assets sold in securitizations~~
~~i. The accounting for and disclosure about collateral that can be sold or repledged.~~

~~The Board concluded that those requests to reconsider certain provisions of Statement 125 were appropriate and added a project to amend Statement 125 to its agenda in March 1997. This Statement is the result. To present the amended accounting standards for transfers of financial assets more clearly, this Statement replaces Statement 125. However, most of the provisions of Statement 125 have been carried forward without reconsideration.~~

g. Paragraph 8A and 8B are added as follows under the heading "Accounting for Transfers and Servicing of Financial Assets":

8A. The objective of paragraph 9 and related implementation guidance is to determine whether a transferor and its **consolidated affiliates** included in the financial statements being presented have surrendered control over transferred financial assets. This determination must consider the transferor's continuing involvement in the transferred financial assets and requires the use of judgment that must consider all arrangements or agreements made contemporaneously with, or in contemplation of, the transfer, even if they were not entered into at the time of the transfer.

8B. The requirements of paragraph 9 apply to transfers of an entire financial asset, transfers of a group of entire financial assets, and transfers of a **participating interest** in an entire financial asset (all of which are referred to collectively in this Statement as *transferred financial assets*). A participating interest has all of the following characteristics:

a. From the date of the transfer, it represents a proportionate (pro rata) ownership interest in an entire financial asset. The percentage of ownership interests held by the transferor in the entire financial asset may vary over time, while the entire financial asset remains outstanding as long as the resulting portions held by the transferor (including any participating interest retained by the transferor, its consolidated affiliates included in the financial statements being presented, or its **agents**) and the transferee(s) meet the other characteristics of a participating interest. For example, if the transferor's interest in an entire financial asset changes because it subsequently sells another interest in the entire financial asset, the interest held initially and subsequently by the transferor must meet the definition of a participating interest.
b. From the date of the transfer, all cash flows received from the entire financial asset are divided proportionately among the participating interest holders in an amount equal to their share of ownership. Cash flows allocated as compensation for services performed, if any, shall not be included in that determination provided those cash flows are not subordinate to the proportionate cash flows of the participating interest and are not significantly above an amount that would fairly compensate a substitute service provider, should one be required, which includes the profit that would be demanded in the marketplace. In addition, any cash flows received by the transferor as **proceeds** of the transfer of the participating interest shall be excluded from the determination of proportionate cash flows provided that the transfer does not result in the transferor receiving an ownership interest in the financial asset that permits it to receive disproportionate cash flows.
c. The rights of each participating interest holder (including the transferor in its role as a participating interest holder) have the same priority, and no participating interest holder's interest is subordinated to the interest of another participating interest holder. That priority does not change in the event of bankruptcy or other receivership of the transferor, the original debtor, or any other participating interest holder. Participating interest holders have no recourse to the transferor (or its consolidated affiliates included in the financial statements being presented or its agents) or to each other, other than **standard representations and warranties,** ongoing contractual obligations to service the entire financial asset and administer the transfer contract, and contractual obligations to share in any set-off benefits received by any participating interest holder. That is, no participating interest holder is entitled to receive cash before any other participating interest holder under its contractual rights as a participating interest holder. For example, if a participating interest holder also is the servicer of the entire financial asset and receives cash in its role as servicer, that arrangement would not violate this requirement.
d. No party has the right to pledge or exchange the entire financial asset unless all participating interest holders agree to pledge or exchange the entire financial asset.

If a transfer of a portion of an entire financial asset meets the definition of a participating interest, the transferor shall apply the guidance in paragraph 9. If a transfer of a portion of a financial asset does not meet the definition of a participating interest, the transferor and transferee shall account for the transfer in accordance with the guidance in paragraph 12. However, if the transferor transfers an entire financial asset in portions that do not individually meet the participating interest definition, paragraph 9 shall be applied to the entire financial asset once all portions have been transferred.

h. Paragraph 9:

A transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset ~~financial assets (or all or a portion of a financial asset)~~ in which the transferor surrenders control over those financial assets shall be accounted for as a sale ~~to the extent that consideration other than **beneficial interests** in the transferred assets is received in exchange. The transferor has surrendered control over transferred assets~~ if and only if *all of the following conditions* are met:

a. The transferred financial assets have been isolated from the transferor—put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership ~~(paragraphs 27 and 28)~~. Transferred financial assets are isolated in bankruptcy or other receivership only if the transferred financial assets would be beyond the reach of the powers of a bankruptcy trustee or other receiver for the transferor or any of its consolidated affiliates included in the financial statements being presented. For multiple step transfers, an entity that is designed to make remote the possibility that it would enter bankruptcy or other receivership (bankruptcy-remote entity) is not considered a consolidated affiliate for purposes of performing the isolation analysis. Notwithstanding the isolation analysis, each entity involved in the transfer is subject to the applicable guidance on whether it must be consolidated (paragraphs 27–28 and 80–84).

b. Each transferee (or, if the transferee is an entity whose sole purpose is to engage in securitization or asset-backed financing activities and that entity is constrained from pledging or exchanging the assets it receives ~~a qualifying SPE (paragraph 35)~~, each third-party holder of its beneficial interests) has the right to pledge or exchange the assets (or beneficial interests) it received, and no condition both constrains the transferee (or third-party holder of its beneficial interests) from taking advantage of its right to pledge or exchange and provides more than a trivial benefit to the transferor (paragraphs 29–33~~29–34~~).

c. The transferor, its consolidated affiliates included in the financial statements being presented, or its agents do~~es~~ not maintain effective control over the transferred financial assets or third-party beneficial interests related to those transferred assets (paragraph 46A). Examples of a transferor's effective control over the transferred financial assets include, but are not limited to ~~through either~~ (1) an agreement that both entitles and obligates the transferor to repurchase or redeem them before their maturity (paragraphs 47–49), ~~or~~ (2) an agreement that provides the transferor with both the ~~ability to unilaterally~~ **unilateral ability** to cause the holder to return specific financial assets and a more-than-trivial benefit attributable to that ability, other than through a **cleanup call** (paragraphs 50–54), or (3) an agreement that permits the transferee to require the transferor to repurchase the transferred financial assets at a price that is so favorable to the transferee that it is probable that the transferee will require the transferor to repurchase them (paragraph 54A).

i. Paragraph 10, as amended, and the heading preceding it:

Accounting for Transfers of Participating Interests

~~Upon completion of any transfer of financial assets, the transferor shall:~~

~~a. Initially recognize and measure at fair value, if practicable (paragraph 71), servicing assets and servicing liabilities that require recognition under the provisions of paragraph 13~~

~~b. Allocate the previous carrying amount between the assets sold, if any, and the interests that continue to be held by the transferor, if any, based on their relative fair values at the date of transfer (paragraphs 56–60)~~

~~c. Continue to carry in its statement of financial position any interest it continues to hold in the transferred assets, including, if applicable, beneficial interests in assets transferred to a qualifying SPE in a **securitization** (paragraphs 73–84), and any **undivided interests** (paragraphs 58 and 59).~~

Upon completion[2a] of a transfer of a participating interest that satisfies the conditions to be accounted for as a sale (paragraph 9), the transferor (**seller**) shall:

a. Allocate the previous carrying amount of the entire financial asset between the participating interests sold and the participating interest that continues to be held by the transferor on the basis of their relative fair values at the date of the transfer (paragraphs 58 and 60)
b. Derecognize the participating interest(s) sold
c. Recognize and initially measure at fair value servicing assets, servicing liabilities, and any other assets obtained and liabilities incurred in the sale (such as cash) (paragraphs 61–64)
d. Recognize in earnings any gain or loss on the sale
e. Report any participating interest or interests that continue to be held by the transferor as the difference between the previous carrying amount of the entire financial asset and the amount derecognized.

The transferee shall recognize the participating interest(s) obtained, other assets obtained, and any liabilities incurred and initially measure them at fair value.

[2a]Although a transfer of securities may not be considered to be completed until the settlement date, this Statement does not modify other generally accepted accounting principles (GAAP), including FASB Statement No. 35, *Accounting and Reporting by Defined Benefit Pension Plans,* and AICPA Statements of Position and Audit and Accounting Guides for certain industries that require accounting at the trade date for certain contracts to purchase or sell securities.

j. Paragraph 10A is added as follows:

Upon completion of a transfer of participating interests that does not satisfy the conditions to be accounted for as a sale, the guidance in paragraph 12 shall be applied.

k. Paragraph 11, as amended, its related footnote 3, and the heading preceding it:

Accounting for Transfers of an Entire Financial Asset or Group of Entire Financial Assets

Upon completion[3] of a transfer of an entire financial asset~~s~~ or a group of entire financial assets that satisfies the conditions to be accounted for as a sale (paragraph 9), the transferor (seller) shall:

a. Derecognize ~~all~~ the transferred financial assets ~~sold~~
~~b. Recognize all assets obtained and liabilities incurred in consideration as **proceeds** of the sale, including cash, put or call options held or written (for example, guarantee or recourse obligations), forward commitments (for example, commitments to deliver additional receivables during the revolving periods of some securitizations), swaps (for example, provisions that convert interest rates from fixed to variable), and servicing assets and servicing liabilities, if applicable (paragraphs 56, 57, and 61–67)~~
c. Recognize and ~~I~~initially measure at fair value servicing assets, servicing liabilities, and any other assets obtained (including a transferor's beneficial interest in the transferred financial assets) and liabilities incurred[3a] in the sale (paragraphs 56, 57, and 61–65)~~a sale or, if it is not practicable to estimate the fair value of an asset or a liability, apply alternative measures (paragraphs 71 and 72)~~
d. Recognize in earnings any gain or loss on the sale.

The transferee shall recognize all assets obtained and any liabilities incurred and initially measure them at fair value~~ (in aggregate, presumptively the price paid)~~.

[3]See footnote 2a.~~Although a transfer of securities may not be considered to have reached completion until the settlement date, this Statement does not modify other generally accepted accounting principles, including FASB Statement No. 35, *Accounting and Reporting by Defined Benefit Pension Plans,* and AICPA Statements of Position and audit and accounting Guides for certain industries, that require accounting at the trade date for certain contracts to purchase or sell securities.~~

[3a]Some assets that might be obtained and liabilities that might be incurred include cash, put or call options that are held or written (for example, guarantee or recourse obligations), forward commitments (for example, commitments to deliver additional receivables during the revolving periods of some securitizations), and swaps (for example, provisions that convert interest rates from fixed to variable).

l. Paragraph 11A is added as follows:

Upon completion of a transfer of an entire financial asset or a group of entire financial assets that does not satisfy the conditions to be accounted for as a sale in its entirety, the guidance in paragraph 12 shall be applied.

m. Paragraph 12 and the heading preceding it:

Secured Borrowing

If a transfer of an entire financial asset~~s~~, a group of entire financial assets, or a participating interest in an entire financial asset ~~in exchange for cash or other consideration (other than beneficial interests in the transferred assets)~~ does not meet the ~~criteria~~ conditions for a sale in paragraph 9~~,~~ or if a transfer of a portion of an entire financial asset does not meet the definition of a participating interest (paragraph 8B), the transferor and transferee shall account for the transfer as a secured borrowing with pledge of collateral (paragraph 15). The transferor shall continue to report the transferred financial assets in its statement of financial position with no change in their measurement (that is, basis of accounting).

n. Paragraph 13, as amended:

An entity shall recognize and initially measure at fair value~~, if practicable,~~ a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in either ~~any~~ of the following situations:

a. A servicer's transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset ~~the servicer's financial assets~~ that meets the requirements for sale accounting; or

~~b. A transfer of the servicer's financial assets to a qualifying SPE in a **guaranteed mortgage securitization** in which the transferor retains all of the resulting securities and classifies them as either available-for-sale securities or trading securities in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*~~

c. An acquisition or assumption of a servicing obligation that does not relate to financial assets of the servicer or its consolidated affiliates included in the financial statements being presented.

An entity that transfers its financial assets ~~to a qualifying SPE in a guaranteed mortgage securitization~~ to an unconsolidated entity in a transfer that qualifies as a sale in which the transferor ~~retains all of~~ obtains the resulting securities and classifies them as debt securities held-to-maturity in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* may either separately recognize its servicing assets or servicing liabilities or report those servicing assets or servicing liabilities together with the asset being serviced.

o. Paragraph 13A, as added:

An entity shall subsequently measure each class of servicing assets and servicing liabilities using one of the following methods:

a. *Amortization method:* Amortize servicing assets or servicing liabilities in proportion to and over the period of estimated net servicing income (if servicing revenues exceed servicing costs) or net servicing loss (if servicing costs exceed servicing revenues), and assess servicing assets or servicing liabilities for impairment or increased obligation based on fair value at each reporting date

b. *Fair value measurement method:* Measure servicing assets or servicing liabilities at fair value at each reporting date and report changes in fair value of servicing assets and servicing liabilities in earnings in the period in which the changes occur.

The election described in this paragraph shall be made separately for each class of servicing assets and servicing liabilities. An entity shall apply the same subsequent measurement method to each servicing asset and servicing liability in a class. Classes of servicing assets and servicing liabilities shall be identified based on (a) the availability of market inputs used in determining the fair value of servicing assets or servicing liabilities, (b) an entity's method for managing the risks of its servicing assets or servicing liabilities, or (c) both. Once an entity elects the fair value measurement method for a class of servicing assets and servicing liabilities, that election shall not be reversed (paragraph 63). ~~If it is not practicable to initially measure a servicing asset or servicing liability at fair value, an entity shall initially recognize the servicing asset or servicing liability in accordance with paragraph 71 and shall include it in a class subsequently measured using the amortization method.~~

p. Paragraph 14, as amended:

Financial assets, except for instruments that are within the scope of Statement 133, that can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment shall be subsequently measured like investments in debt securities classified as available-for-sale or trading under Statement 115. Examples of such financial assets include, but are not limited to, interest-only strips, other beneficial interests~~Interest-only strips, other interests that continue to be held by a transferor in securitizations~~, loans, or other receivables~~, or other financial assets that can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment, except for instruments that are within the scope of Statement 133, shall be subsequently measured like investments in debt securities classified as available-for-sale or trading under Statement 115, as amended (paragraph 362)~~.

q. Paragraph 16A, as added, its related footnote 5a, and the headings preceding and following it:

~~**Disclosures for Public Entities**~~

16A. ~~In addition to the disclosures required by other standards, a public entity[5a] shall provide disclosures as required in Appendix B of FASB Staff Position (FSP) FAS 140-4 and FIN 46(R)-8, *Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities*~~ The principal objectives of the disclosures required by this Statement are to provide users of the financial statements with an understanding of all of the following:

a. A transferor's continuing involvement (as defined in the glossary of this Statement), if any, with transferred financial assets
b. The nature of any restrictions on assets reported by an entity in its statement of financial position that relate to a transferred financial asset, including the carrying amounts of those assets
c. How servicing assets and servicing liabilities are reported under this Statement
d. For transfers accounted for as sales when a transferor has continuing involvement with the transferred financial assets and for transfers of financial assets accounted for as secured borrowings, how the transfer of financial assets affects a transferor's financial position, financial performance, and cash flows.

Those objectives apply regardless of whether this Statement requires specific disclosures. The specific disclosures required by this Statement are minimum requirements and an entity may need to supplement the required disclosures specified in paragraph 17 depending on the facts and circumstances of a transfer, the nature of an entity's continuing involvement with the transferred financial assets, and the effect of an entity's continuing involvement on the transferor's financial position, financial performance, and cash flows. Disclosures required by other U.S. generally accepted accounting principles (GAAP) for a particular form of continuing involvement shall be considered when determining whether the disclosure objectives of this Statement have been met.

~~**Disclosures for Nonpublic Entities**~~

~~[5a]The following definitions of public and nonpublic shall be applied in assessing whether an entity is public or nonpublic:~~

~~**Nonpublic entity**—Any entity other than one (a) whose debt or equity securities trade in a public market either on a stock exchange (domestic or foreign) or in the over-the-counter market, including securities quoted only locally or regionally, (b) that is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets), (c) that makes a filing with a regulatory agency in preparation for the sale of any class of debt or equity securities in a public market, or (d) that is controlled by an entity covered by (a), (b), or (c).~~

~~*Conduit debt securities* refers to certain limited-obligation revenue bonds, certificates of participation, or similar debt instruments issued by a state or local governmental entity for the express purpose of providing financing for a specific third party (the conduit bond obligor) that is not a part of the state or local government's financial reporting entity. Although conduit debt securities bear the name of the governmental entity that issues them, the governmental entity often has no obligation for such debt beyond the resources provided by a lease or loan agreement with the third party on whose behalf the securities are issued. Further, the conduit bond obligor is responsible for any future financial reporting requirements.~~

~~**Public entity**—Any entity that does not meet the definition of a *nonpublic entity*.~~

r. Paragraphs 16B–16E are added as follows:

16B. Disclosures required by this Statement may be reported in the aggregate for similar transfers if separate reporting of each transfer would not provide more useful information to financial statement users. A transferor shall disclose how similar transfers are aggregated. A transferor shall distinguish transfers that are accounted for as sales from transfers that are accounted for as secured borrowings. In determining whether to aggregate the disclosures for multiple transfers, the reporting entity shall consider quantitative and qualitative information about the characteristics of the transferred financial assets. For example, consideration should be given, but not limited, to the following:

a. The nature of the transferor's continuing involvement, if any
b. The types of financial assets transferred
c. Risks related to the transferred financial assets to which the transferor continues to be exposed after the transfer and the change in the transferor's risk profile as a result of the transfer
d. The requirements of FSP SOP 94-6-1, *Terms of Loan Products That May Give Rise to a Concentration of Credit Risk.*

16C. The disclosures shall be presented in a manner that clearly and fully explains to financial statement users the transferor's risk exposure related to the transferred financial assets and any restrictions on the assets of the entity. An entity shall determine, in light of the facts and circumstances, how much detail it must provide to satisfy the disclosure requirements of this Statement and how it aggregates information for assets with different risk characteristics. The entity must strike a balance between obscuring important information as a result of too much aggregation and excessive detail that may not assist financial statement users to understand the entity's financial position. For example, an entity shall not obscure important information by including it with a large amount of insignificant detail. Similarly, an entity shall not disclose information that is so aggregated that it obscures important differences between the different types of involvement or associated risks.

16D. The disclosures in paragraph 17(f) of this Statement apply to transfers accounted for as sales when the transferor has continuing involvement with transferred financial assets as a result of a securitization, asset-backed financing arrangement, or a similar transfer. If specific disclosures are required for a particular form of the transferor's continuing involvement by other U.S. GAAP, the transferor shall provide the information required in paragraphs 17(f)(1)(a) and 17(f)(2)(a) of this Statement with a cross-reference to the separate notes to financial statements so a financial statement user can understand the risks retained in the transfer. The entity need not provide each specific disclosure required in paragraphs 17(f)(1)(b), 17(f)(2)(a)(i)–(iv), and 17(f)(2)(b)–(e) if the disclosure is not required by other U.S. GAAP and the objectives of paragraph 16A are met. For example, if the transferor's only form of continuing involvement is a derivative, the entity shall provide the disclosures required in paragraphs 17(f)(1)(a) and 17(f)(2)(a) of this Statement and the disclosures about derivatives required by applicable U.S. GAAP. In addition, the entity would evaluate whether the other disclosures in paragraph 17(f) are necessary for the entity to meet the objectives in paragraph 16A.

16E. To apply the disclosures in paragraph 17, an entity shall consider all involvements by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents to be involvements by the transferor.

s. Paragraph 17, as amended, and its related footnotes 6–10:

An entity shall disclose the following:

a. For collateral:
   (1) If the entity has entered into repurchase agreements or securities lending transactions, its policy for requiring collateral or other security.
   (2) If the entity has pledged any of its assets as collateral that are not reclassified and separately reported in the statement of financial position pursuant to paragraph 15(a), the carrying amounts and classifications of both those assets and associated liabilities as of the date of the latest statement of financial position presented, including qualitative information about the relationship(s) between those assets and associated liabilities. For example, if assets are restricted solely to satisfy a specific obligation, the carrying amounts of those assets and associated liabilities, including a description of the nature of restrictions placed on the assets, shall be disclosed.
   (3) If the entity has accepted collateral that it is permitted by contract or custom to sell or repledge, the fair value as of the date of each statement of financial position presented of that collateral and of the portion of that collateral that it has

sold or repledged, and information about the sources and uses of that collateral.

b. For in-substance defeasance of debt:

~~b.~~(1) If debt was considered to be extinguished by in-substance defeasance under the provisions of FASB Statement No. 76, *Extinguishment of Debt,* prior to the effective date of Statement 125,[6] a general description of the transaction and the amount of debt that is considered extinguished at the end of each ~~the~~ period ~~so long as~~ that debt remains outstanding.

~~c. If assets are set aside after the effective date of Statement 125 solely for satisfying scheduled payments of a specific obligation, a description of the nature of restrictions placed on those assets.~~

~~d. If it is not practicable to estimate the fair value of certain assets obtained or liabilities incurred in transfers of financial assets during the period, a description of those items and the reasons why it is not practicable to estimate their fair value.~~

~~e~~c. For all servicing assets and servicing liabilities:

(1) Management's basis for determining its classes of servicing assets and servicing liabilities (paragraph 13A).

(2) A description of the risks inherent in servicing assets and servicing liabilities and, if applicable, the instruments used to mitigate the income statement effect of changes in fair value of the servicing assets and servicing liabilities. (Disclosure of quantitative information about the instruments used to manage the risks inherent in servicing assets and servicing liabilities, including the fair value of those instruments at the beginning and end of the period, is encouraged but not required.)

(3) The amount of **contractually specified servicing fees** ~~(as defined in the glossary)~~, late fees, and ancillary fees earned for each period for which results of operations are presented, including a description of where each amount is reported in the statement of income.

(4) Quantitative and qualitative information about the assumptions used to estimate the fair value (for example, discount rates, anticipated credit losses, and prepayment speeds). (An entity that provides quantitative information about the instruments used to manage the risks inherent in the servicing assets and servicing liabilities, as encouraged by paragraph 17(c)(2), also is encouraged, but not required, to disclose quantitative and qualitative information about the assumptions used to estimate the fair value of those instruments.)

~~f~~d. For servicing assets and servicing liabilities subsequently measured at fair value:

(1) For each class of servicing assets and servicing liabilities, the activity in the balance of servicing assets and the activity in the balance of servicing liabilities (including a description of where changes in fair value are reported in the statement of income for each period for which results of operations are presented), including, but not limited to, the following:

(a) The beginning and ending balances

(b) Additions (through purchases of servicing assets, assumptions of servicing obligations, and recognition of servicing obligations that result from transfers of financial assets)

(c) Disposals

(d) Changes in fair value during the period resulting from:

(i) Changes in valuation inputs or assumptions used in the valuation model

(ii) Other changes in fair value and a description of those changes

(e) Other changes that affect the balance and a description of those changes.

~~(2) A description of the valuation techniques or other methods used to estimate the fair value of servicing assets and servicing liabilities. If a valuation model is used, the description shall include the methodology and model validation procedures, as well as quantitative and qualitative information about the assumptions used in the valuation model (for example, discount rates and prepayment speeds). (An entity that provides~~

~~quantitative information about the instruments used to manage the risks inherent in the servicing assets and servicing liabilities, as encouraged by paragraph 17(e)(2), is also encouraged, but not required, to disclose a description of the valuation techniques, as well as quantitative and qualitative information about the assumptions used to estimate the fair value of those instruments.)~~

~~g~~e. For servicing assets and servicing liabilities subsequently amortized in proportion to and over the period of estimated net servicing income or loss and assessed for impairment or increased obligation:

(1) For each class of servicing assets and servicing liabilities, the activity in the balance of servicing assets and the activity in the balance of servicing liabilities (including a description of where changes in the carrying amount are reported in the statement of income for each period for which results of operations are presented), including, but not limited to, the following:

(a) The beginning and ending balances
(b) Additions (through purchases of servicing assets, assumptions of servicing obligations, and recognition of servicing obligations that result from transfers of financial assets)
(c) Disposals
(d) Amortization
(e) Application of valuation allowance to adjust carrying value of servicing assets
(f) Other-than-temporary impairments
(g) Other changes that affect the balance and a description of those changes.

(2) For each class of servicing assets and servicing liabilities, the fair value of recognized servicing assets and servicing liabilities at the beginning and end of the period~~ if it is practicable to estimate the value~~.

~~(3) A description of the valuation techniques or other methods used to estimate fair value of the servicing assets and servicing liabilities. If a valuation model is used, the description shall include the methodology and model validation procedures, as well as quantitative and qualitative information about the assumptions used in the valuation model (for example, discount rates, and prepayment speeds). (An entity that provides quantitative information about the instruments used to manage the risks inherent in the servicing assets and servicing liabilities, as encouraged by paragraph 17(e)(2), is also encouraged, but not required, to disclose a description of the valuation techniques as well as quantitative and qualitative information about the assumptions used to estimate the fair value of those instruments.)~~

(~~4~~3) The risk characteristics of the underlying financial assets used to stratify recognized servicing assets for purposes of measuring impairment in accordance with paragraph 63.

(~~5~~4) The activity by class in any valuation allowance for impairment of recognized servicing assets—including beginning and ending balances, aggregate additions charged and recoveries credited to operations, and aggregate write-downs charged against the allowance—for each period for which results of operations are presented.

~~h~~f. ~~If the entity has securitized~~For securitizations, asset-backed financing arrangements, and similar transfers accounted for as sales when the transferor has continuing involvement (as defined in the glossary) with the transferred financial assets~~ during any period presented and accounts for that transfer as a sale, for each major asset type (for example, mortgage loans, credit card receivables, and automobile loans)~~:

(1) For each income statement presented:~~Its accounting policies for initially measuring the interests that continue to be held by the transferor, if any, and servicing assets or servicing liabilities, if any, including the methodology (whether quoted market price, prices based on sales of similar assets and liabilities, or prices based on valuation techniques) used in determining their fair value.~~

(~~2~~a) The characteristics of the transfer ~~securitizations~~ (including a description of the transferor's continuing involvement with the transferred financial assets, and the nature and initial fair value of the assets obtained as proceeds and the liabilities incurred in the transfer ~~including, but not limited to, servicing, recourse, and restrictions on interests that continue to be held by the transferor~~) and the gain or loss from sale of transferred financial assets ~~in securitizations~~. For initial fair value measurements of assets obtained and liabilities incurred in the transfer, the following information:

(i) The level within the fair value hierarchy (as described in FASB Statement No. 157, *Fair Value Measurements*) in which the fair value measurements in their entirety fall, segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3)

(~~3~~ii) The key inputs and assumptions[7] used in measuring the fair value of assets obtained and liabilities incurred as a result of the sale ~~interests that continue to be held by the transferor and servicing assets or servicing liabilities, if any, at the time of securitization~~ that relate to the transferor's continuing involvement (including, at a minimum, but not limited to, and if applicable, quantitative information about discount rates, expected prepayments including the expected weighted-average life of prepayable financial assets,[8] and anticipated credit losses, ~~if applicable~~including expected static pool losses[8a])[8b]

(iii) The valuation technique(s) used to measure fair value.

(~~4~~b) Cash flows between a transferor and transferee, ~~the securitization SPE and the transferor, unless reported separately elsewhere in the financial statements or notes~~ (including proceeds from new transfers ~~securitizations~~, proceeds from collections reinvested in revolving-period transfers ~~securitizations~~, purchases of previously transferred financial assets ~~delinquent or foreclosed loans~~, servicing fees, and cash flows received ~~on~~ from a transferor's beneficial interests ~~that continue to be held by the transferor~~).

~~i.~~(2) For each statement of financial position presented, regardless of when the transfer occurred: ~~If the entity has interests that continue to be held by the transferor in financial assets that it has securitized or servicing assets or servicing liabilities relating to assets that it has securitized, at the date of the latest statement of financial position presented, for each major asset type (for example, mortgage loans, credit card receivables, and automobile loans):~~

(a) Qualitative and quantitative information about the transferor's continuing involvement with transferred financial assets that provides financial statement users with sufficient information to assess the reasons for the continuing involvement and the risks related to the transferred financial assets to which the transferor continues to be exposed after the transfer and the extent that the transferor's risk profile has changed as a result of the transfer (including, but not limited to, credit risk, interest rate risk, and other risks), including:

(i) The total principal amount outstanding, the amount that has been derecognized, and the amount that continues to be recognized in the statement of financial position

(ii) The terms of any arrangements that could require the transferor to provide financial support (for example, liquidity arrangements and obligations to purchase assets) to the transferee or its beneficial interest holders, including a description of any events or circumstances that could expose the transferor to loss and the amount of the maximum exposure to loss

(iii) Whether the transferor has provided financial or other support during the periods presented that it was not previously contractually required to provide to the transferee or its beneficial interest holders, including when the transferor assisted the transferee or its beneficial interest holders in obtaining support, including:

(1) The type and amount of support

(2) The primary reasons for providing the support

(iv) Information is encouraged about any liquidity arrangements, guarantees, and/or other commitments provided by third parties related to the transferred financial assets that may affect the transferor's exposure to loss or risk of the related transferor's interest.

(b~~1~~) The entity's ~~Its~~ accounting policies for subsequently measuring ~~those interests~~assets or liabilities that relate to the continuing involvement with the transferred financial assets~~, including the methodology (whether quoted market price, prices based on sales of similar assets and liabilities, or prices based on valuation techniques) used in determining their fair value~~

(c~~2~~) The key inputs and assumptions[8c] used in ~~subsequently~~ measuring the fair value of ~~those interests~~ assets or liabilities that relate to the transferor's continuing involvement (including, at a minimum, but not limited to, and if applicable, quantitative information about discount rates, expected prepayments including the expected weighted-average life of prepayable financial assets,[8d] and anticipated credit losses, including expected static pool losses~~,~~[9] ~~if applicable~~)[9a]

(d~~3~~) For the transferor's interests in the transferred financial assets, a~~A~~ sensitivity analysis or stress test showing the hypothetical effect on the fair value of those interests (including any servicing assets or servicing liabilities) of two or more unfavorable variations from the expected levels for each key assumption that is reported under paragraph 17(f)(2)(c) above independently from any change in another key assumption, and a description of the objectives, methodology, and limitations of the sensitivity analysis or stress test

(e~~4~~) Information about the asset quality of transferred financial assets and any other assets that it manages together with them. This information shall be separated between assets that have been derecognized and assets that continue to be recognized in the statement of financial position. This information is intended to provide financial statement users with an understanding of the risks inherent in the transferred financial assets as well as in other assets and liabilities that it manages together with transferred financial assets. For example, information for receivables shall include, but is not limited to:~~For the securitized assets and any other financial assets that it manages together with them:~~[10]

~~(a) The total principal amount outstanding, the portion that~~

~~has been derecognized, and the portion that continues to be recognized in each category reported in the statement of financial position, at the end of the period~~

(~~b~~i) Delinquencies at the end of the period

(~~c~~ii) Credit losses, net of recoveries, during the period.

~~(Disclosure of average balances during the period is encouraged, but not required.)~~

g. Disclosure requirements for transfers of financial assets accounted for as secured borrowings:

(1) The carrying amounts and classifications of both assets and associated liabilities recognized in the transferor's statement of financial position at the end of each period presented, including qualitative information about the relationship(s) between those assets and associated liabilities. For example, if assets are restricted solely to satisfy a specific obligation, the carrying amounts of those assets and associated liabilities, including a description of the nature of restrictions placed on the assets.

[6]Statement 125 applied to transfers and servicing of financial assets and extinguishments of liabilities occurring after December 31, 1996 (after December 31, 1997, for transfers affected by FASB Statement No. 127, *Deferral of the Effective Date of Certain Provisions of FASB Statement No. 125*) and on or before March 31, 2001. Statement 127 deferred until December 31, 1997, 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.~~Refer to footnote 11 to paragraph 19.~~

[7]If an entity has aggregated ~~made~~ multiple ~~securitizations of the same major asset type~~ transfers during a period in accordance with paragraphs 16B and 16C, it may disclose the range of assumptions.

[8]The weighted-average life of prepayable assets in periods (for example, months or years) can be calculated by multiplying the principal collections expected in each future period by the number of periods until that future period, summing those products, and dividing the sum by the initial principal balance.

[8a]Expected static pool losses can be calculated by summing the actual and projected future credit losses and dividing the sum by the original balance of the pool of assets.

[8b]The timing and amount of future cash flows for transferor's interests in transferred financial assets are commonly uncertain, especially if those interests are subordinate to more senior beneficial interests. Thus, estimates of future cash flows used for a fair value measurement depend heavily on assumptions about default and prepayment of all the financial assets transferred, because of the implicit credit or prepayment risk enhancement arising from the subordination.

[8c]See footnote 7.

[8d]See footnote 8.

[9]~~Expected static pool losses can be calculated by summing the actual and projected future credit losses and dividing the sum by the original balance of the pool of assets~~See footnote 8a.

[9a]~~The timing and amount of future cash flows for retained interests in securitizations are commonly uncertain, especially if those interests are subordinate to more senior beneficial interests. Thus, estimates of future cash flows used for a fair value measurement depend heavily on assumptions about default and prepayment of all the assets securitized, because of the implicit credit or prepayment risk enhancement arising from subordination~~See footnote 8b.

~~[10]Excluding securitized assets that an entity continues to service but with which it has no other continuing involvement.~~

t. Paragraph 26A is added as follows:

Paragraph 8A of this Statement states that the objective of paragraph 9 and related implementation guidance is to determine whether a transferor and its consolidated affiliates included in the financial statements being presented have surrendered control over transferred financial assets. As a result, in determining whether the transferor has surrendered control over transferred financial assets, the transferor must first consider whether the transferee would be consolidated by the transferor. Therefore, if all other provisions of this Statement are met with respect to a particular transfer, and the transferee would be consolidated by the transferor, then the transferred financial assets would not be treated as having been sold in the financial statements being presented. However, if the transferee is a consolidated subsidiary of the transferor (its parent), the transferee shall recognize the transferred financial assets in its separate company financial statements, unless the nature of the transfer is a secured borrowing with a pledge of collateral (for example, a repurchase agreement that would not be accounted for as a sale under the provisions of paragraphs 47–49).

u. Paragraphs 26B and 26C and the heading preceding them are added as follows:

Unit of Account

26B. Paragraph 8B establishes the unit of account to which the sale accounting conditions in paragraph 9 shall be applied. Paragraph 8B states that paragraph 9 shall be applied to transfers of an entire financial asset, transfers of a group of entire financial assets, and transfers of a participating interest in an entire financial asset. Inherent in that principle is that to be eligible for sale accounting an entire financial asset cannot be divided into components before a transfer unless all of the components meet the definition of a participating interest.

26C. The legal form of the asset and what the asset conveys to its holders shall be considered in determining what constitutes an entire financial asset. The following examples illustrate the application of what constitutes an entire financial asset:

a. A loan to one borrower in accordance with a single contract that is transferred to a securitization entity before securitization shall be considered an entire financial asset. Similarly, a beneficial interest in securitized financial assets after the securitization process has been completed shall be considered an entire financial asset. In contrast, a transferred interest in an individual loan shall not be considered an entire financial asset; however, if the transferred interest meets the definition of a participating interest, the participating interest would be eligible for sale accounting.
b. In a transaction in which the transferor creates an interest-only strip from a loan and transfers the interest-only strip, the interest-only strip does not meet the definition of an entire financial asset (and an interest-only strip does not meet the definition of a participating interest; therefore, sale accounting would be precluded). In contrast, if an entire financial asset is transferred to a securitization entity that it does not consolidate and the transfer meets the conditions for sale accounting, the transferor may obtain an interest-only strip as proceeds from the sale. An interest-only strip received as proceeds of a sale is an entire financial asset for purposes of evaluating any future transfers that could then be eligible for sale accounting.
c. If multiple advances are made to one borrower in accordance with a single contract (such as a line of credit, credit card loan, or a construction loan), an advance on that contract would be a separate unit of account if the advance retains its identity, does not become part of a larger loan balance, and is transferred in its entirety. However, if the transferor transfers an advance in its entirety and the advance loses its identity and becomes part of a larger loan balance, the transfer would be eligible for sale accounting only if the transfer of the advance does not result in the transferor retaining any interest in the larger balance or if the transfer results in the transferor's interest in the larger balance meeting the definition of a participating interest. Similarly, if the transferor transfers an interest in an advance that has lost its identity, the interest must be a participating interest in the larger balance to be eligible for sale accounting.

v. Paragraphs 26D–26H and the heading preceding them are added as follows:

Participating Interests in an Entire Financial Asset

26D. Paragraph 8B(b) requires that all cash flows received from the entire financial asset be divided among the participating interest holders (including any interest retained by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents) in proportion to their share of ownership. That is, the participating interest definition does not allow for the allocation of specified cash flows unless each cash flow is proportionately allocated to the participating interest holders. For example, in the case of an individual loan in which the borrower is required to make a contractual payment that consists of a principal amount and interest amount on the loan, the transferor and transferee shall share in the principal and interest payments on the basis of their proportionate ownership interest in the loan. In contrast, if the transferor is entitled to receive an amount that represents the principal payments and the transferee is entitled to receive an amount that represents the interest payments on the loan, that arrangement would not be consistent with the participating interest definition because the transferor and transferee do not share proportionately in the cash flows received from the loan. In other cases, a transferor may transfer a portion of an individual loan that represents either a senior interest or a junior interest in an individual loan. In both of those cases, the transferor would account for the transfer as a secured borrowing because the senior interest or junior interest in the loan do not meet the requirements to be participating interests (see paragraph 26H).

26E. Paragraph 8B(b) states that cash flows allocated as compensation for services performed, if any, shall not be included in that determination provided that those cash flows are not subordinate to the proportionate cash flows of the participating interest and are not significantly above an amount that would fairly compensate a substitute service provider, should one be required, including any profit that would be demanded in the marketplace. Cash flows allocated as compensation for services performed that are significantly above an amount that would fairly compensate a substitute service provider would result in a disproportionate division of cash flows of the entire financial asset among the participating interest holders and, therefore, would preclude the portion of a transferred financial asset from meeting the definition of a participating interest. Examples of cash flows that are compensation for services performed include loan origination fees (as defined by FASB Statement No. 91, *Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases*) paid by the borrower to the transferor, fees necessary to arrange and complete the transfer paid by the transferee to the transferor, and fees for servicing the financial asset.

26F. The transfer of a portion of an entire financial asset may result in a gain or loss on the transfer when the contractual interest rate on the entire financial asset differs from the market rate at the time of transfer. Paragraph 8B(b) states that any cash flows received by the transferor as proceeds of a transfer of a participating interest shall be excluded from the determination of whether the cash flows of the participating interest are proportionate provided that the transfer does not result in the transferor receiving an ownership interest in the financial asset that permits it to receive disproportionate cash flows. For example, if the transferor transfers an interest in an entire financial asset and the transferee agrees to incorporate the excess interest (between the contractual interest rate on the financial asset and the market interest rate at the date of transfer) into the contractually specified servicing fee, the excess interest would likely result in the conveyance of an interest-only strip to the transferor from the transferee. An interest-only strip would result in a disproportionate division of cash flows of the financial asset among the participating interest holders and would preclude the portion from meeting the definition of a participating interest.

26G. Paragraph 8B(c) requires that the rights of each participating interest holder (including the transferor in its role as participating interest holder) have the same priority and that no participating holder's interest is subordinated to the interest of another participating interest holder. In certain transfers, recourse is provided to the transferee that requires the transferor to reimburse any premium paid by the transferee if the underlying financial asset is prepaid within a defined time frame of the transfer date. Such recourse would preclude the transferred portion from meeting the definition of a participating interest. However, once the recourse provision expires, the transferred portion shall be reevaluated to determine if it meets the participating interest definition.

26H. Paragraph 8B(c) also requires that participating interest holders have no recourse to the transferor (or its consolidated affiliates included in the financial statements being presented or its agents) or to each other, other than standard representations and warranties, ongoing contractual obligations to service the entire financial asset and administer the transfer contract, and contractual obligations to share in any set-off benefits. Recourse in the form of an independent third-party guarantee shall be excluded from the evaluation of whether the participating interest definition is met. Similarly, cash flows allocated to a third-party guarantor for the guarantee fee shall be excluded from the determination of whether the cash flows are divided proportionately among the participating interest holders.

w. Paragraph 27:

The nature and extent of supporting evidence required for an assertion in financial statements that an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset (which are referred to collectively in this Statement as *transferred financial assets*) ~~transferred financial assets~~ have been isolated—put presumptively beyond the reach of the transferor, any of its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented, and its creditors, either by a single transaction or a series of transactions taken as a whole—depend on the facts and circumstances. All available evidence that either supports or questions an assertion shall be considered, including~~. That consideration includes making judgments about~~ whether the contract or circumstances permit the transferor to revoke the transfer. It also may include ~~making judgments about the kind of~~ consideration of the legal consequences of the transfer in the jurisdiction in which bankruptcy or other receivership would take place~~into which a transferor or SPE might be placed~~, whether a transfer of financial assets would likely be deemed a true sale at law (as described in paragraph 27A) or otherwise isolated (as described in paragraph 27B), whether the transferor is affiliated with the transferee, and other factors pertinent under applicable law. Derecognition of transferred financial assets is appropriate only if the available evidence provides reasonable assurance that the transferred financial assets would be beyond the reach of the powers of a bankruptcy trustee or other receiver for the transferor or any of its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented and its creditors ~~**consolidated affiliate of the transferor** that is not a special-purpose corporation or other entity designed to make remote the possibility that it would enter bankruptcy or other receivership~~ (paragraph 83(c)).

x. Paragraphs 27A and 27B are added as follows:

27A. In the context of U.S. bankruptcy laws, a true sale opinion from an attorney is often required to support a conclusion that transferred financial assets are isolated from the transferor, any of its consolidated affiliates included in the financial statements being presented, and its creditors. In addition, a nonconsolidation opinion is often required if the transfer is to an affiliated entity. In the context of U.S. bankruptcy laws:

a. A true sale opinion is an attorney's conclusion that the transferred financial assets have been sold and are beyond the reach of the transferor's creditors and that a court would conclude that the transferred financial assets would not be included in the transferor's bankruptcy estate.

b. A nonconsolidation opinion is an attorney's conclusion that a court would recognize that an entity holding the transferred financial assets exists separately from the transferor. Additionally, a nonconsolidation opinion is an attorney's conclusion that a court would not order the substantive consolidation of the assets and liabilities of the entity holding the transferred financial assets and the assets and liabilities of the transferor (and its consolidated affiliates included in the financial statements being presented) in the event of the transferor's bankruptcy or receivership.

A legal opinion may not be required if a transferor has a reasonable basis to conclude that the appropriate legal opinion(s) would be given if requested. For example, the transferor might reach a conclusion without consulting an attorney if (1) the transfer is a routine transfer of financial assets that does not result in any continuing involvement by the transferor or (2) the transferor had experience with other transfers with similar facts and circumstances under the same applicable laws and regulations.

27B. For entities that are subject to other possible bankruptcy, conservatorship, or other receivership procedures (for example, banks subject to receivership by the Federal Deposit Insurance Corporation [FDIC]) in the United States or other jurisdictions, judgments about whether transferred financial assets have been isolated need to be made in relation to the powers of bankruptcy courts or trustees, conservators, or receivers in those jurisdictions.

y. Paragraph 28:

Whether securitizations isolate transferred financial assets may depend on such factors as whether the securitization is accomplished in one step or multiple ~~two~~ step~~s~~ transfers (paragraphs 80–84). Some ~~Many~~ common financial transactions, for example, typical repurchase agreements and securities lending transactions, may isolate transferred financial assets from the transferor, although they may not meet the other ~~criteria~~ conditions for surrender of control (paragraph 9).

z. Paragraph 29:

Sale accounting is allowed under paragraph 9(b) only if each transferee (or, if the transferee is an entity whose sole purpose is to engage in securitization or asset-backed financing arrangements and that entity is constrained from pledging or exchanging the assets it receives, each third-party holder of its beneficial interests) has the right to pledge~~,~~ or ~~the right to~~ exchange~~,~~ the ~~transferred~~ assets or beneficial interests it received, ~~but constraints on that right also matter~~ and no condition both constrains the transferee (or third-party holder of its beneficial interests) from taking advantage of its right to pledge or exchange and provides more than a trivial benefit to the transferor. Many transferor-imposed or other conditions on a transferee's right to pledge or exchange ~~a transferred asset~~ both constrain a transferee from pledging or exchanging ~~the transferred assets~~ and, through that constraint, provide more than a trivial benefit to the transferor. Judgment is required to assess whether a particular condition results in a constraint. Judgment also is required to assess whether a constraint provides a more-than-trivial benefit to the transferor. If the transferee is an entity whose sole purpose is to engage in securitization or asset-backed financing activities, that entity may be constrained from pledging or exchanging the transferred financial assets to protect the rights of beneficial interest holders in the financial assets of the entity. Paragraph 9(b) requires that the transferor look through the constrained entity to determine whether each third-party holder of its beneficial interests has the right to pledge or exchange the beneficial interests that it holds. The considerations in paragraphs 29A–32 apply to the transferee or the third-party holders of its beneficial interests in an entity that is constrained from pledging or exchanging the assets it receives and whose sole purpose is to engage in securitization or asset-backed financing activities.~~For example, a provision in the transfer contract that prohibits selling or pledging a transferred loan receivable not only constrains the transferee but also provides the transferor with the more-than-trivial benefits of knowing who has the asset, a prerequisite to repurchasing the asset, and of being able to block the asset from finding its way into the hands of a competitor for the loan customer's business or someone that the loan customer might consider an undesirable creditor. Transferor-imposed contractual constraints that narrowly limit timing or terms, for example, allowing a transferee to pledge only on the day assets are obtained or only on terms agreed with the transferor, also constrain the transferee and presumptively provide the transferor with more-than-trivial benefits.~~

aa. Paragraph 29A is added as follows:

> Some conditions may constrain a transferee from pledging or exchanging the financial asset and may provide the transferor with more than a trivial benefit. For example, a provision that prohibits selling or pledging a transferred loan receivable not only constrains the transferee but also provides the transferor with the more-than-trivial benefit of knowing who holds the financial asset (a prerequisite to repurchasing the financial asset) and of being able to block the financial asset from being transferred to a competitor for the loan customer's business. Transferor-imposed contractual constraints that narrowly limit timing or terms, for example, allowing a transferee to pledge only on the day assets are obtained or only on terms agreed to with the transferor, also constrain the transferee and presumptively provide the transferor with more-than-trivial benefits. In some circumstances in which the transferor has no continuing involvement with the transferred financial assets, some conditions may constrain a transferee from pledging or exchanging the financial assets. If the transferor, its consolidated affiliates included in the financial statements being presented, and its agents have no continuing involvement with the transferred financial assets, the condition under paragraph 9(b) is met. For example, if a transferor receives only cash in return for the transferred financial assets and the transferor, its consolidated affiliates included in the financial statements being presented, and its agents have no continuing involvement with the transferred financial assets, sale accounting is allowed under paragraph 9(b) even if the transferee entity is significantly limited in its ability to pledge or exchange the transferred assets.

bb. Paragraph 30:

> However, some conditions may ~~do~~ not constrain a transferee from pledging or exchanging the transferred financial asset ~~and therefore do not preclude a transfer subject to such a condition from being accounted for as a sale~~. For example, a transferor's right of first refusal on the occurrence of a bona fide offer to the transferee from a third party presumptively would not constrain a

transferee~~,~~. This is because ~~that~~ the right in itself does not enable the transferor to compel the transferee to sell the ~~assets~~ financial asset and the transferee would be in a position to receive the sum offered by exchanging the financial asset, albeit possibly from the transferor rather than the third party. Further examples of conditions that presumptively would not constrain a transferee for purposes of this Statement include (a) a requirement to obtain the transferor's permission to sell or pledge that is not to be unreasonably withheld, (b) a prohibition on sale to the transferor's competitor if other potential willing buyers exist, (c) a regulatory limitation such as on the number or nature of eligible transferees (as in the case of securities issued under Securities Act Rule 144A or debt placed privately), and (d) illiquidity, for example, the absence of an active market. ~~Judgment~~ However, judgment is required to assess the significance of some conditions. For example, a prohibition on sale to the transferor's competitor would be a ~~significant~~ constraint if that competitor were the only potential willing buyer other than the transferor.

cc. Paragraph 32 and the heading preceding it:

Transferor's Rights or Obligations to Reacquire Transferred Assets or Beneficial Interests

Some rights or obligations to reacquire transferred financial assets or beneficial interests both constrain the transferee and provide more than a trivial benefit to the transferor, thus precluding sale accounting under paragraph 9(b). ~~For example, a~~ A **freestanding call** option written by a transferee to the transferor ~~benefits~~ may benefit the transferor and, if the transferred financial assets are not readily obtainable in the marketplace, is likely to constrain a transferee because ~~it~~ the transferee might have to default if the call was exercised and ~~it~~ the transferee had ~~exchanged or~~ pledged or exchanged the financial assets. For example, if a transferor in a securitization transaction has a call option to repurchase third-party beneficial interests at the price paid plus a stated return, that arrangement conveys more than a trivial benefit to the transferor (paragraphs 50 and 51). If the third-party holders of its beneficial interests are constrained from pledging or exchanging their beneficial interests due to that call option, the transferor would be precluded from accounting for the transfer of financial assets to the securitization entity as a sale. ~~A~~ Similarly, a freestanding forward purchase-sale contract between the transferor and the transferee on transferred financial assets not readily obtainable in the marketplace would benefit the transferor and is likely to constrain a transferee in much the same manner. ~~Judgment is necessary to assess constraint and benefit. For example, put options written to the transferee generally do not constrain it, but a put option on a not-readily-obtainable asset may benefit the transferor and effectively constrain the transferee if the option is sufficiently deep-in-the-money when it is written that it is probable that the transferee will exercise it and the transferor will reacquire the transferred asset. In contrast, a sufficiently out-of-the-money call option held by the transferor may not constrain a transferee if it is probable when the option is written that it will not be exercised. Freestanding~~ Alternatively, freestanding rights to reacquire transferred assets that are readily obtainable presumptively do not constrain the transferee from ~~exchanging or~~ pledging or exchanging them and thus do not preclude sale accounting under paragraph 9(b).

dd. Paragraph 33 and its related footnote 15:

Other rights or obligations to reacquire transferred financial assets, regardless of whether they constrain the transferee, may result in the transferor's maintaining effective control over the transferred financial assets, as discussed in paragraphs 46A~~50~~–54A, thus precluding sale accounting under paragraph 9(c)~~(2)~~.~~[15]~~ For example, an **attached call** in itself would not constrain a transferee who is able, by exchanging or pledging the asset subject to that call, to obtain substantially all of its economic benefits. However, an attached call could result in the transferor's maintaining effective control over the transferred asset(s) because the attached call gives the transferor the unilateral ability to cause whoever holds that specific asset to return it.

~~[15]And it is necessary to consider the overall effect of related rights and obligations in assessing such matters as whether a transferee is constrained or a transferor has maintained effective control. For example, if the transferor or its affiliate or agent is the servicer for the transferred asset and is empowered to decide to put the asset up for sale, and has the right of first refusal, that combination would place the transferor in position to unilaterally cause the return of a specific transferred asset and thus maintain the transferor's effective control of the transferred asset as discussed in paragraphs 9(c)(2) and 50.~~

ee. Paragraphs 34 and 35, as amended, 36–39, 40, as amended, and 41–46, their related footnotes, and their related headings are deleted because of the removal of the qualifying special-purpose entity concept.

ff. Paragraph 46A is added as follows, and the heading preceding it:

~~Maintaining~~ Effective Control over Transferred Financial Assets or Beneficial Interests

Judgment is required to assess whether the transferor maintains effective control over transferred financial assets or third-party beneficial interests. The transferor must evaluate whether a combination of multiple arrangements maintains effective control of transferred financial assets. When the transferee issues beneficial interests in the transferred financial assets, the evaluation of whether the transferor maintains effective control over the transferred financial assets also shall consider whether the transferor maintains effective control over the transferred financial assets through its control over the third-party beneficial interests. To assess whether the transferor maintains effective control over the transferred financial assets, all continuing involvement by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents shall be considered continuing involvement by the transferor. When assessing effective control, the transferor only considers the involvements of an agent when the agent acts for and on behalf of the transferor. In other words, if the transferor and transferee have the same agent, the agent's activities on behalf of the transferee would not be considered in the transferor's evaluation of whether it has effective control over a transferred financial asset. For example, an investment manager may act as a fiduciary (agent) for both the transferor and the transferee; therefore, the transferor need only consider the involvements of the investment manager when it is acting on its behalf.

gg. Paragraphs 47–49 and the heading preceding them:

Agreement to Repurchase or Redeem Transferred Financial Assets

47. An agreement that both entitles and obligates the transferor to repurchase or redeem transferred financial assets from the transferee maintains the transferor's effective control over those assets as described in ~~under~~ paragraph 9(c)(1)~~, and the transfer is therefore to be accounted for as a secured borrowing, if and only if~~ when all of the following conditions are met:

a. The financial assets to be repurchased or redeemed are the same or substantially the same as those transferred (paragraph 48).
b. The transferor is able to repurchase or redeem them on substantially the agreed terms, even in the event of default by the transferee (paragraph 49).
c. The agreement is to repurchase or redeem them before maturity, at a fixed or determinable price.
d. The agreement is entered into contemporaneously with, or in contemplation of, ~~concurrently with~~ the transfer.

48. To be substantially the same,[18] the financial asset that was transferred and the financial asset that is to be repurchased or redeemed need to have all of the following characteristics:

a. The same primary obligor (except for debt guaranteed by a sovereign government, central bank, government-sponsored enterprise or agency thereof, in which case the guarantor and the terms of the guarantee must be the same)
b. Identical form and type so as to provide the same risks and rights
c. The same maturity (or in the case of mortgage-backed pass-through and pay-through securities, similar remaining weighted-average maturities that result in approximately the same market yield)
d. Identical contractual interest rates
e. Similar assets as collateral
f. The same aggregate unpaid principal amount or principal amounts within accepted "good delivery" standards for the type of security involved.

49. To be able to repurchase or redeem financial assets on substantially the agreed terms, even in the event of default by the transferee, a transferor must at all times during the contract term have obtained cash or other collateral sufficient to fund substantially all of the cost of purchasing replacement financial assets from others.

hh. Paragraphs 50–54 and the heading preceding them:

Unilateral Ability to~~Ability to Unilaterally~~ Cause the Return of Specific Transferred Financial Assets

50. ~~Some rights to reacquire transferred assets (or to acquire beneficial interests in transferred assets held by a qualifying SPE), regardless of whether they constrain the transferee, may result in the transferor's maintaining effective control over the transferred assets through the **unilateral ability** to cause the return of specific transferred assets. Such rights preclude sale accounting under paragraph 9(c)(2). For example, an **attached call** in itself would not constrain a transferee who is able, by exchanging or pledging the asset subject to that call, to obtain substantially all of its economic benefits. An attached call could result, however, in the transferor's maintaining effective control over the transferred asset(s) because the attached call gives the transferor the ability to unilaterally cause whoever holds that specific asset to return it. In contrast, transfers of financial assets subject to calls embedded by the issuers of the financial instruments, for example, callable bonds or prepayable mortgage loans, do not preclude sale accounting. Such an **embedded call** does not result in the transferor's maintaining effective control, because it is the issuer rather than the transferor who holds the call.~~ A transferor maintains effective control over transferred financial assets when the transferor has the unilateral ability to cause the holder to return specific financial assets and that ability provides more than a trivial benefit to the transferor. A cleanup call, however, is permitted as an exception to that general principle. A call on a transferred financial asset provides the transferor with effective control over that financial asset if, under its price and other terms, the call provides the transferor with the unilateral ability to reclaim the transferred financial asset and conveys more than a trivial benefit to the transferor. A call or other right conveys more than a trivial benefit if the price to be paid is fixed, determinable, or otherwise potentially advantageous, unless because that price is so far out of the money or for other reasons it is probable when the option is written that the transferor will not exercise it. A transferor's unilateral ability to cause a securitization entity to return to the transferor or otherwise dispose of specific transferred financial assets, for example, in response to its decision to exit a market or a particular activity, would provide the transferor with effective control over the transferred financial assets if it provides more than a trivial benefit to the transferor. However, a call on readily obtainable assets at fair value may not provide the transferor with more than a trivial benefit. (Paragraph 53 provides an example in which, due to the combination of arrangements, the transferor would maintain effective control.)

51. Effective control over transferred financial assets can be present even if the right to reclaim is indirect. For example, if a call allows a transferor to buy back the beneficial interests at a fixed price, the transferor may maintain effective control of the financial assets underlying those beneficial interests. If the transferee is ~~a qualifying SPE, it has met the conditions in paragraph 35(d) and therefore must~~ an entity whose sole purpose is to engage in securitization or asset-backed financing activities, that entity may be constrained from choosing to ~~exchange or~~ pledge or exchange the transferred financial assets. In that circumstance, any call held by the transferor on third-party beneficial interests is effectively ~~attached to~~ an attached call on the transferred financial assets. ~~and could—depending~~ Depending on the price and other terms of the call~~—~~, the transferor may maintain ~~the transferor's~~ effective control over the transferred financial assets.~~ through the ability to unilaterally cause the transferee to return specific assets. For example, a transferor's unilateral ability to cause a qualifying SPE to return to the transferor or otherwise dispose of specific transferred assets at will or, for example, in response to its decision to exit a market or a particular activity, could provide the transferor with effective control over the transferred assets.~~

52. ~~A call that is attached to transferred assets maintains the transferor's effective control over those assets if, under its price and other terms, the call conveys more than a trivial benefit to the transferor. Similarly, any unilateral right to reclaim specific assets transferred to a qualifying SPE maintains the transferor's effective control over those assets if the right conveys more than a trivial benefit to the transferor. A call or other right conveys more than a trivial benefit if the price to be paid is fixed, determinable, or otherwise potentially advantageous, unless because~~

~~that price is so far out of the money or for other reasons it is probable when the option is written that the transferor will not exercise it. Thus, for example, a call on specific assets transferred to a qualifying SPE at a price fixed at their principal amount maintains the transferor's effective control over the assets subject to that call. Effective control over transferred assets can be present even if the right to reclaim is indirect. For example, if an embedded call allows a transferor to buy back the beneficial interests of a qualifying SPE at a fixed price, then the transferor remains in effective control of the assets underlying those beneficial interests. A cleanup call, however, is permitted as an exception to that general principle.~~An **embedded call** would not result in the transferor's maintaining effective control because it is the issuer rather than the transferor who holds the call and the call does not provide more than a trivial benefit to the transferor. For example, a call embedded by the issuer of a callable bond or the borrower of a prepayable mortgage loan would not provide the transferor with effective control over the transferred financial asset.

53. A right to reclaim specific transferred financial assets by paying their fair value when reclaimed generally does not maintain effective control~~, because~~ when it does not convey a more than trivial benefit to the transferor. However, a transferor has maintained effective control if it has such a right and also holds the residual interest in the transferred financial assets. For example, if a transferor holds the residual interest in securitized financial assets and can reclaim ~~such~~ the transferred financial assets at termination of the securitization entity ~~qualifying SPE~~ by purchasing them in an auction, and thus at what might appear to be fair value, then sale accounting for the transfer of those financial assets it can reclaim would be precluded. Such circumstances provide the transferor with a more than trivial benefit and effective control over the financial assets, because it can pay any price it chooses in the auction and recover any excess paid over fair value through its residual interest in the transferred financial assets.

54. ~~A transferor that has a right to reacquire transferred assets from a qualifying SPE does not maintain effective control if the reclaimed assets would be randomly selected and the amount of the assets reacquired is sufficiently limited (paragraph 87(a)), because that would not be a right to reacquire *specific* assets. Nor does~~ Some removal-of-account provisions do not result in the transferor's maintaining effective control, as discussed in paragraphs 85–88. For example, a transferor does not maintain effective control through an obligation to reacquire transferred financial assets from a securitization entity ~~qualifying SPE~~ if the reacquisition ~~transfer~~ could occur only after a specified failure of the servicer to properly service the transferred financial assets that could result in the loss of a third-party guarantee ~~(paragraph 42(a))~~ or only after ~~a BIH other than the transferor, its affiliate, or its agent requires a qualifying SPE~~ third-party beneficial interest holders require a securitization entity to repurchase that beneficial interest ~~(paragraph 44(b))~~, because the transferor could not cause that reacquisition *unilaterally*.

ii. Paragraph 54A and the heading preceding it are added as follows:

Arrangements to Reacquire Transferred Financial Assets

A transferor maintains effective control over the transferred financial asset as described in paragraph 9(c)(3) through an agreement that permits the transferee to require the transferor to repurchase the transferred financial asset at a price that is so favorable to the transferee at the date of the transfer that it is probable that the transferee will require the transferor to repurchase the transferred financial asset. For example, a put option written to the transferee generally does not provide the transferor with effective control over the transferred financial asset. However, a put option that is sufficiently deep in the money when it is written would provide the transferor effective control over the transferred financial asset because it is probable that the transferee will exercise the option and the transferor will be required to repurchase the transferred financial asset. In contrast, a sufficiently out-of-the-money put option held by the transferee would not provide the transferor with effective control over the transferred financial asset if it is probable when the option is written that the option will not be exercised. Likewise, a put option held by the transferee at fair value would not provide the transferor with effective control over the transferred financial asset.

jj. Paragraph 55 and the heading preceding it:

Changes That Result in the Transferor's Regaining Control of Financial Assets Sold

A change in law~~, status of the transferee as a qualifying SPE,~~ or other circumstance may result in a transferred portion of an entire financial asset no longer meeting the conditions of a participating interest (paragraph 8B) or the transferor's regaining control of transferred financial assets after a transfer that was previously accounted for ~~appropriately~~ as a sale~~having been sold~~, because one or more of the conditions in paragraph 9 are no longer met. Such changes~~a change~~, unless ~~it arises~~ they arise solely from ~~either~~ the initial application of this Statement, from consolidation of an entity involved in the transfer at a subsequent date (paragraph 55A), or from a change in market prices (for example, an increase in price that moves into-the-money a freestanding call on a non-readily-obtainable transferred financial asset that was originally sufficiently out-of-the-money that it was judged not to constrain the transferee), are ~~is~~ accounted for in the same manner as a purchase of the transferred financial assets from the former transferee(s) in exchange for liabilities assumed (paragraph 10 or 11). After that change, the transferor recognizes in its financial statements those transferred financial assets together with liabilities to the former transferee(s) or ~~BIHs in those assets (paragraph 38)~~beneficial interest holders of the former transferee(s). The transferor initially measures those transferred financial assets and liabilities at fair value on the date of the change, as if the transferor purchased the transferred financial assets and assumed the liabilities on that date. The former transferee would derecognize the transferred financial assets on that date, as if it had sold the transferred financial assets in exchange for a receivable from the transferor.

kk. Paragraph 55A is added as follows:

If a transferor subsequently consolidates an entity involved in a transfer that was accounted for as a sale, it shall account for the consolidation in accordance with applicable consolidation accounting guidance.

ll. Paragraph 56, as amended:

The proceeds from a sale of financial assets consist of the cash and any other assets obtained, including beneficial interests and separately recognized servicing assets, in the transfer less any liabilities incurred, including separately recognized servicing liabilities. Any asset obtained ~~that is not an interest in the transferred asset~~ is part of the proceeds from the sale. Any liability incurred, even if it is related to the transferred financial assets, is a reduction of the proceeds. Any derivative financial instrument entered into concurrently with a transfer of financial assets is either an asset obtained or a liability incurred and part of the proceeds received in the transfer. All proceeds and reductions of proceeds from a sale shall be initially measured at fair value~~, if practicable~~.

mm. Paragraph 57, as amended:

Company A transfers ~~sells~~ entire loans with a carrying amount of $1,000 to an unconsolidated securitization entity and receives proceeds with a fair value of $~~1,100~~ 1,030~~and a carrying amount of $1,000~~, and the transfer is accounted for as a sale.[18a] Company A undertakes no servicing responsibilities ~~but obtains an option to purchase from the transferee loans similar to the loans sold (which are readily obtainable in the marketplace)~~ and assumes a limited recourse obligation to repurchase delinquent loans.

Company A agrees to provide the transferee a return at a floating rate of interest even though the contractual terms of the loan are fixed rate in nature (that provision is effectively an interest rate swap).

Fair Values	
Cash proceeds	$ 1,050
Interest rate swap asset	40
~~Call option~~	~~70~~
Recourse obligation	60

Net Proceeds	
Cash received	$ 1,050
Plus: ~~Call option~~	~~70~~
Interest rate swap asset	40
Less: Recourse obligation	(60)
Net proceeds	$ 1,030~~$1,100~~

Gain on Sale	
Net proceeds	$ 1,030~~$1,100~~
Less: Carrying amount of loans sold	(1,000)
Gain on sale	$ 30~~$ 100~~

Journal Entry		
Cash	1,050	
Interest rate swap asset	40	
~~Call option~~	~~70~~	
Loans		1,000
Recourse obligation		60
Gain on sale		~~100~~30
To record transfer		

[18a]For purposes of this illustration, the transaction described in this paragraph is assumed to meet the conditions for a sale in paragraph 9 of this Statement. There is no assurance or presumption that this transaction or any other transaction in the examples in this Statement would meet the conditions in paragraph 9.

nn. Paragraphs 58 and 59, as amended, and the heading preceding them:

Participating Interests in Financial Assets That Continue to Be Held by a Transferor

58. ~~Other~~ Participating interests in ~~transferred~~ financial assets that continue to be held by a transferor~~—those that~~ are not part of the proceeds of the transfer~~—are interests that continue to be held by a transferor over which the transferor has not relinquished control. Interests that continue to be held by a transferor~~, and the carrying amount of those participating interests shall be measured at the date of the transfer by allocating the previous carrying amount between the participating interests transferred and ~~assets~~ sold, ~~if any,~~ and the participating interests that are not transferred and continue to be held by a transferor, based on their relative fair values. ~~Allocation procedures shall be applied to all transfers in which interests continue to be held by a transferor, even those that do not qualify as sales. Examples of interests that continue to be held by a transferor include securities backed by the transferred assets, undivided interests, and cash reserve accounts and residual interests in~~

~~securitization trusts. If a transferor cannot determine whether an asset is an interest that continues to be held by a transferor or proceeds from the sale, the asset shall be treated as proceeds from the sale and accounted for in accordance with paragraph 56.~~

~~59. If the interests that continue to be held by a transferor are subordinate to more senior interests held by others, that subordination may concentrate most of the risks inherent in the transferred assets into the interests that continue to be held by a transferor and shall be taken into consideration in estimating the fair value of those interests. For example, if the amount of the gain recognized, after allocation, on a securitization with a subordinated interest that continues to be held by a transferor is greater than the gain that would have been recognized had the entire asset been sold, the transferor needs to be able to identify why that can occur. Otherwise, it is likely that the effect of subordination to a senior interest has not been adequately considered in the determination of the fair value of the subordinated interest that continues to be held by a transferor.~~

oo. Paragraph 60, as amended, and the heading preceding it:

Illustration—Recording Transfers of Participating ~~Partial~~ Interests

Company B transfers ~~sells~~ a ~~pro rata~~ nine-tenths participating interest in a loan ~~loans~~ with a fair value of $1,100 and a carrying amount of $1,000, and the transfer is accounted for as a sale.[18b] The servicing contract has a fair value of zero ~~There is no servicing asset or liability,~~ because Company B estimates that the **benefits of servicing** are just adequate to compensate it for its servicing responsibilities.

Fair Values	
Cash proceeds for nine-tenths participating interest sold ($1,100 × 9/10)	$990
One-tenth participating interest that continues to be held by ~~a~~ the transferor ~~[($990 ÷ 9/10) × 1/10]~~ ($1,100 × 1/10)	110

Allocated Carrying Amount Based on Relative Fair Values

	Fair Value	Percentage of Total Fair Value	Allocated Carrying Amount
Nine-tenths participating interest sold	$ 990	90	$ 900
One-tenth participating interest that continues to be held by ~~a~~ the transferor	110	10	100
Total	$ 1,100	100	$ 1,000

Gain on Sale	
Net proceeds	$ 990
Less: Carrying amount of loans sold	(900)
Gain on sale	$ 90

Journal Entry		
Cash	990	
Loans		900
Gain on sale		90
To record transfer		

[18b]See footnote 18a.

pp. Paragraphs 61 and 62, as amended, 62A, as added, 63, as amended, and 64:

61. Servicing of mortgage loans, credit card receivables, or other financial assets commonly includes, but is not limited to, collecting principal, interest, and escrow payments from borrowers; paying taxes and insurance from escrowed funds; monitoring delinquencies; executing foreclosure if necessary; temporarily investing funds pending distribution; remitting fees to guarantors, trustees, and others providing services; and accounting for and remitting principal and interest payments to the holders of beneficial interests or participating interests in the financial assets. Servicing is inherent in all financial assets; it becomes a distinct asset or liability for accounting purposes only in the circumstances described in paragraph 62. If a transferor sells a participating interest in an entire financial asset, it would recognize a servicing asset or a servicing liability only related to the participating interest sold.

62. An entity that undertakes a contract to service financial assets shall recognize either a servicing asset or a servicing liability~~,~~ each time it undertakes an obligation to service a financial asset that (a) results from a servicer's transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset ~~the servicer's financial assets~~ that meets the requirements for sale accounting~~, (b) results from a transfer of the servicer's financial assets to a qualifying SPE in a guaranteed mortgage securitization in which the transferor retains all of the resulting securities and classifies them as either available-for-sale securities or trading securities in accordance with Statement 115,~~ or (be) is acquired or assumed and the servicing obligation does not relate to financial assets of the servicer or its consolidated affiliates included in the financial statements being presented. However, if the transferor transfers the assets to an unconsolidated entity in a transfer that qualifies as a sale in which the transferor~~in a guaranteed mortgage securitization, retains all of~~ obtains the resulting securities, and classifies them as debt securities held-to-maturity in accordance with Statement 115, the servicing asset or servicing liability may be reported together with the asset being serviced and not recognized separately. A servicer of financial assets commonly receives the benefits of servicing—revenues from contractually specified servicing fees, a portion of the interest from the financial assets, late charges, and other ancillary sources, including "float," all of which it is entitled to receive only if it performs the servicing—and incurs the costs of servicing the financial assets. Typically, the benefits of servicing are expected to be more than **adequate compensation** to a servicer for performing the servicing, and the contract results in a servicing asset. However, if the benefits of servicing are not expected to adequately compensate a servicer for performing the servicing, the contract results in a servicing liability. (A servicing asset may become a servicing liability, or vice versa, if circumstances change, and the initial measure for servicing may be zero if the benefits of servicing are just adequate to compensate the servicer for its servicing responsibilities.) A servicer would account for its servicing contract that qualifies for separate recognition as a servicing asset or a servicing liability initially measured at its fair value regardless of whether explicit consideration was exchanged.

62A. A servicer that transfers or securitizes financial assets in a transaction that does not meet the requirements for sale accounting and is accounted for as a secured borrowing with the underlying financial assets remaining on the transferor's balance sheet shall not recognize a servicing asset or a servicing liability.~~However, if a transferor enters into a servicing contract when the transferor transfers mortgage loans in a guaranteed mortgage securitization, retains all the resulting securities, and classifies those securities as either available-for-sale securities or~~

~~trading securities in accordance with Statement 115, the transferor shall separately recognize a servicing asset or a servicing liability.~~

63. A servicer that recognizes a servicing asset or servicing liability shall account for the contract to service financial assets separately from those financial assets, as follows:

a. Report servicing assets separately from servicing liabilities in the statement of financial position (paragraph 13B).
b. Initially measure servicing assets and servicing liabilities at fair value~~, if practicable~~ (paragraphs 10(c)~~, 11(b),~~ and 11(c)~~, 71, and 72~~).
c. Account separately for rights to future interest income from the serviced assets that exceed contractually specified servicing fees. Those rights are not servicing assets; they are financial assets, effectively interest-only strips to be accounted for in accordance with paragraph 14 of this Statement. (Interest-only strips preclude a portion of a financial asset from meeting the definition of a participating interest; see paragraph 26F.)
d. Identify classes of servicing assets and servicing liabilities based on (1) the availability of market inputs used in determining the fair value of servicing assets and servicing liabilities, (2) an entity's method for managing the risks of its servicing assets and servicing liabilities, or (3) both.
e. Subsequently measure each class of separately recognized servicing assets and servicing liabilities either at fair value or by amortizing the amount recognized in proportion to and over the period of estimated net servicing income for assets (the excess of servicing revenues over servicing costs) or the period of estimated net servicing loss for servicing liabilities (the excess of servicing costs over servicing revenues). Different elections can be made for different classes of servicing assets and servicing liabilities. An entity may make an irrevocable decision to subsequently measure a class of servicing assets and servicing liabilities at fair value at the beginning of any fiscal year. Once a servicing asset or a servicing liability is reported in a class of servicing assets and servicing liabilities that an entity elects to subsequently measure at fair value, that servicing asset or servicing liability cannot be placed in a class of servicing assets and servicing liabilities that is subsequently measured using the amortization method. Changes in fair value should be reported in earnings for servicing assets and servicing liabilities subsequently measured at fair value (paragraph 13A(b)).
f. Subsequently evaluate and measure impairment of each class of separately recognized servicing assets that are subsequently measured using the amortization method described in paragraph 13A(a) as follows:
   (1) Stratify servicing assets within a class based on one or more of the predominant risk characteristics of the underlying financial assets. Those characteristics may include financial asset type,[19] size, interest rate, date of origination, term, and geographic location.
   (2) Recognize impairment through a valuation allowance for an individual stratum. The amount of impairment recognized separately shall be the amount by which the carrying amount of servicing assets for a stratum exceeds their fair value. The fair value of servicing assets that have not been recognized shall not be used in the evaluation of impairment.
   (3) Adjust the valuation allowance to reflect changes in the measurement of impairment subsequent to the initial measurement of impairment. Fair value in excess of the carrying amount of servicing assets for that stratum, however, shall not be recognized. This Statement does not address when an entity should record a direct write-down of recognized servicing assets.
g. For servicing liabilities subsequently measured using the amortization method, if subsequent events have increased the fair value of the liability above the carrying amount, for example, because of significant changes in the amount or timing of actual or expected future cash flows relative to the cash flows previously projected, the servicer shall revise its earlier estimates and recognize the increased obligation as a loss in earnings (paragraph 13A).

64. As indicated above, transferors sometimes agree to take on servicing responsibilities when the future benefits of servicing are not expected to adequately compensate them for performing that servicing. In that circumstance, the result is

a servicing liability rather than a servicing asset. For example, if in the transaction illustrated in paragraph 57 the transferor had agreed to service the loans without explicit compensation and it estimated the fair value of that servicing obligation at $50, net proceeds would be reduced to $980~~1,050~~, gain on sale would become ~~be reduced to $50~~a loss on sale of $20, and the transferor would report a servicing liability of $50.

qq. Paragraphs 65 and 66, as amended:

65. Company C originates $1,000 of loans that yield 10 percent interest income for their estimated lives of 9 years. Company C ~~sells the~~ transfers the entire loans to an unconsolidated entity and the transfer is accounted for as a sale.[19a] ~~$1,000 principal plus the right to receive interest income of 8 percent to another entity for $1,000.~~ Company C receives as proceeds $1,000 cash, a beneficial interest to receive 1 percent of the contractual interest on the loans (an interest-only strip receivable), and an additional 1 percent of the contractual interest as compensation for servicing the loans. ~~Company C will continue to service the loans, and the contract stipulates that its compensation for performing the servicing is the right to receive half of the interest income not sold. The remaining half of the interest income not sold is considered an interest-only strip receivable that Company C classifies as an available-for-sale security. At the date of the transfer, the fair value of the loans is $1,100.~~ The fair values of the servicing asset and the interest-only strip receivable are $40 and $60, respectively.

Fair Values	
Cash proceeds	$ 1,000
Servicing asset	40
Interest-only strip receivable	60

Net Proceeds	
Cash proceeds	$ 1,000
Servicing asset	40
Interest-only strip receivable	60
Net proceeds	$ 1,100~~$ 1,040~~

~~**Carrying Amount Based on Relative Fair Values**~~

	~~Fair Value~~	~~Percentage of Total Fair Value~~	~~Allocated Carrying Amount~~
~~Loans sold~~	~~$ 1,040~~	~~94.55~~	~~$ 945.50~~
~~Interest-only strip receivable~~	~~60~~	~~5.45~~	~~54.50~~
~~Total~~	~~$ 1,100~~	~~100.00~~	~~$ 1,000.00~~

Gain on Sale	
Net proceeds	$ 1,100~~$ 1,040.00~~
Less: Carrying amount of loans sold	(1,000)~~945.50~~
Gain on sale	$ 100~~$ 94.50~~

Journal Entries		
Cash	1,000~~.00~~	
Interest-only strip receivable	60~~54.50~~	
Servicing asset	40~~.00~~	
Loans		1,000~~.00~~
Gain on sale		100~~94.50~~
To record transfer and to recognize interest-only strip receivable and servicing asset		
~~Interest-only strip receivable~~	~~5.50~~	
~~Other comprehensive income~~		~~5.50~~
~~To begin to subsequently measure interest-only strip receivable like an available-for-sale security (paragraph 14)~~		

~~66. The previous illustration demonstrates how a transferor would account for a simple sale in which servicing is obtained. Company C might instead transfer the financial assets to a corporation or a trust that is a qualifying SPE. The qualifying SPE then securitizes the loans by selling beneficial interests to the public. The qualifying SPE pays the cash proceeds to the original transferor, which accounts for the transfer as a sale and derecognizes the financial assets assuming that the criteria in paragraph 9 are met. Securitizations often combine the elements shown in paragraphs 57, 60, and 65, as illustrated below.~~

[19a]See footnote 18a.

rr. Paragraph 67, as amended, and the heading preceding it:

~~***Illustration—Recording Transfers of Partial Interests with Proceeds of Cash, Derivatives, Other Liabilities, and Servicing***~~

~~Company D originates $1,000 of prepayable loans that yield 10 percent interest income for their 9-year expected lives. Company D sells nine-tenths of the principal plus interest of 8 percent to another entity. Company D will continue to service the loans, and the contract stipulates that its compensation for performing the servicing is the 2 percent of the interest income not sold. Company D obtains an option to purchase from the transferee loans similar to the loans sold (which are readily obtainable in the marketplace) and incurs a limited recourse obligation to repurchase delinquent loans. At the date of transfer, the fair value of the loans is $1,100.~~

~~**Fair Values**~~	
~~Cash proceeds~~	~~$ 900~~
~~Call option~~	~~70~~
~~Recourse obligation~~	~~(60)~~
~~Servicing asset~~	~~90~~
~~One-tenth interest that continues to be held by the transferor~~	~~100~~

~~**Net Proceeds**~~	
~~Cash received~~	~~$ 900~~
~~Plus: Servicing asset~~	~~90~~
~~Plus: Call option~~	~~70~~
~~Less: Recourse obligation~~	~~(60)~~
~~Net proceeds~~	~~$ 1,000~~

~~**Carrying Amount Based on Relative Fair Values**~~

	~~Fair Value~~	~~Percentage of Total Fair Value~~	~~Allocated Carrying Amount~~
~~Interest sold~~	~~$ 1,000~~	~~90.9~~	~~$ 909~~
~~One-tenth interest that continues to be held by the transferor~~	~~100~~	~~9.1~~	~~91~~
~~Total~~	~~$ 1,100~~	~~100.0~~	~~$ 1,000~~

~~**Gain on Sale**~~	
~~Net proceeds~~	~~$ 1,000~~
~~Less: Carrying amount of loans sold~~	~~(909)~~
~~Gain on sale~~	~~$ 91~~

~~**Loans Sold**~~	
~~Carrying amount of loans~~	~~$ 1,000~~
~~Less: Allocated carrying amount of interest that continues to be held by the transferor~~	~~(91)~~
~~Loans sold~~	~~$ 909~~

~~**Journal Entries**~~		
~~Cash~~	~~900~~	
~~Call option~~	~~70~~	
~~Servicing asset~~	~~90~~	
~~Loans~~		~~909~~
~~Recourse obligation~~		~~60~~
~~Gain on sale~~		~~91~~
~~To record transfer and to recognize servicing asset, call option, and recourse obligation~~		

ss. Paragraph 71 and the heading preceding it:

~~**If It Is Not Practicable to Estimate Fair Values**~~

~~If it is not practicable to estimate the fair values of assets, the transferor shall record those assets at zero. If it is not practicable to estimate the fair values of liabilities, the transferor shall recognize no gain on the transaction and shall record those liabilities at the greater of:~~

~~a. The excess, if any, of (1) the fair values of assets obtained less the fair values of other liabilities incurred, over (2) the sum of the carrying values of the assets transferred~~

~~b. The amount that would be recognized in accordance with FASB Statement No. 5, *Accounting for Contingencies*, as interpreted by FASB Interpretation No. 14, *Reasonable Estimation of the Amount of a Loss.*~~

tt. Paragraph 72, as amended, and the heading preceding it:

~~***Illustration—Recording Transfers If It Is Not Practicable to Estimate a Fair Value***~~

~~Company E sells loans with a carrying amount of $1,000 to another entity for cash proceeds of $1,050 plus a call option to purchase loans simi-~~

~~lar to the loans sold (which are readily obtainable in the marketplace) and incurs a limited recourse obligation to repurchase any delinquent loans. Company E undertakes an obligation to service the transferred assets for the other entity. In Case 1, Company E finds it impracticable to estimate the fair value of the servicing contract, although it is confident that servicing revenues will be more than adequate compensation for performing the servicing. In Case 2, Company E finds it impracticable to estimate the fair value of the recourse obligation.~~

~~**Fair Values**~~	~~**Case 1**~~	~~**Case 2**~~
~~Cash proceeds~~	~~$ 1,050~~	~~$ 1,050~~
~~Servicing asset~~	~~XX~~ *	~~40~~
~~Call option~~	~~70~~	~~70~~
~~Recourse obligation~~	~~(60)~~	~~XX~~ *
~~Fair value of loans transferred~~	~~1,100~~	~~1,100~~

~~* Not practicable to estimate fair value.~~

~~**Net Proceeds**~~	~~**Case 1**~~	~~**Case 2**~~
~~Cash received~~	~~$ 1,050~~	~~$ 1,050~~
~~Plus: Servicing asset~~	~~XX~~ *	~~40~~
~~Plus: Call option~~	~~70~~	~~70~~
~~Less: Recourse obligation~~	~~(60)~~	~~XX~~ ‡
~~Net proceeds~~	~~$ 1,060~~	~~$ 1,160~~

~~**Gain on Sale**~~	~~**Case 1**~~	~~**Case 2**~~
~~Net proceeds~~	~~$ 1,060~~	~~$ 1,160~~
~~Carrying amount of loans~~	~~1,000~~	~~1,000~~
~~Less: Recourse obligation~~	~~0~~	~~(160)~~ ‡
~~Gain on sale~~	~~$ 60~~	~~$ 0~~

~~**Journal Entries**~~	~~**Case 1**~~		~~**Case 2**~~	
~~Cash~~	~~1,050~~		~~1,050~~	
~~Servicing asset~~	~~0~~ *		~~40~~	
~~Call option~~	~~70~~		~~70~~	
~~Loans~~		~~1,000~~		~~1,000~~
~~Recourse obligation~~		~~60~~		~~160~~ ‡
~~Gain on sale~~		~~60~~		~~0~~
~~To record transfer~~				

~~* Assets shall be recorded at zero if an estimate of the fair value of the assets is not practicable.~~

~~‡ The amount recorded as a liability in this example equals the sum of the known assets less the fair value of the known liabilities, that is, the amount that results in no gain or loss.~~

uu. Paragraphs 73–75, and 76, as amended:

73. Financial assets such as mortgage loans, automobile loans, trade receivables, credit card receivables, and other revolving charge accounts are financial assets commonly transferred in securitizations. Securitizations of mortgage loans may include pools of single-family residential mortgages or other types of real estate mortgage loans, for example, multifamily residential mortgages and commercial property mortgages. Securitizations of loans secured by chattel mortgages on automotive vehicles as well as other equipment (including direct financing or sales-type leases) also are common. Both financial and nonfinancial assets can be securitized; life

insurance policy loans, patent and copyright royalties, and even taxi medallions also have been securitized. But securitizations of nonfinancial assets are outside the scope of this Statement.

74. An originator of a typical securitization (the transferor) transfers a portfolio of financial assets to a securitization entity ~~an SPE~~, commonly a trust. In "pass-through" and "pay-through" securitizations, receivables are transferred to the ~~SPE~~ entity at the inception of the securitization, and no further transfers are made; all cash collections are paid to the holders of beneficial interests in the entity ~~SPE~~. In "revolving-period" securitizations, receivables are transferred at the inception and also periodically (daily or monthly) thereafter for a defined period (commonly three to eight years), referred to as the revolving period. During the revolving period, the ~~SPE~~ entity uses most of the cash collections to purchase additional receivables from the transferor on prearranged terms.

75. Beneficial interests in the securitization entity ~~SPE~~ are sold to investors and the proceeds are used to pay the transferor for the ~~assets~~ transferred financial assets. Those beneficial interests may comprise either a single class having equity characteristics or multiple classes of interests, some having debt characteristics and others having equity characteristics. The cash collected from the portfolio is distributed to the investors and others as specified by the legal documents that established the entity ~~SPE~~.

76. Pass-through, pay-through, and revolving-period securitizations that meet the ~~criteria~~ conditions in paragraph 9 qualify for sale accounting under this Statement, provided that the securitization entity is not consolidated by the transferor or its consolidated affiliates in the financial statements being presented. All financial assets obtained ~~or that continue to be held by a transferor~~ and liabilities incurred by the transferor ~~originator~~ of a securitization that qualifies as a sale shall be recognized and measured as provided in paragraphs 10 and 11; that includes the implicit forward contract to sell additional financial assets ~~new receivables~~ during a revolving period, which may become valuable or onerous to the transferor as interest rates and other market conditions change.

vv. Paragraphs 78 and 79:

78. Gain or loss recognition for revolving-period receivables sold to a securitization trust is limited to receivables that exist and have been sold. Recognition of servicing assets or servicing liabilities for revolving-period receivables is similarly limited to the servicing for the receivables that exist and have been sold~~transferred~~. As new receivables are sold, rights to service them may become assets or liabilities that ~~and~~ are recognized.

~~79. Revolving-period securitizations may use either a discrete trust, used for a single securitization, or a master trust, used for many securitizations. To achieve another securitization using an existing master trust, a transferor first transfers additional receivables to the trust and then sells additional ownership interests in the trust to investors. Adding receivables to a master trust, in itself, is neither a sale nor a secured borrowing under paragraph 9, because that transfer only increases the transferor's beneficial interest in the trust's assets. A sale or secured borrowing does not occur until the transferor receives consideration other than beneficial interests in the transferred assets. Transfers that result in an exchange of cash, that is, either transfers that in essence replace previously transferred receivables that have been collected or sales of beneficial interests to outside investors, are transfers in exchange for consideration other than beneficial interests in the transferred assets and thus are accounted for as sales (if they satisfy all the criteria in paragraph 9) or as secured borrowings.~~

ww. Paragraphs 80 and 81 and 84, and 82 and 83, as amended, and the heading preceding them:

Isolation of Transferred Financial Assets in Securitizations

80. A securitization carried out in one transfer or a series of transfers may or may not isolate the transferred financial assets beyond the reach of the transferor, its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented, and its creditors. Whether it does depends on the structure of the securitization transaction taken as a whole, considering such factors as the type and extent of

further involvement in arrangements to protect investors from credit, ~~and~~ interest rate, and other risks, the availability of other financial assets, and the powers of bankruptcy courts or other receivers. The discussion in paragraphs 81–83 relates only to the isolation condition in paragraph 9(a). The conditions in paragraphs 9(b) and 9(c) also must be considered to determine whether a transferor has surrendered control over the transferred financial assets.

81. In certain securitizations, a corporation that, if it failed, would be subject to the U.S. Bankruptcy Code transfers financial assets to a securitization entity ~~special-purpose trust~~ in exchange for cash. The entity ~~trust~~ raises that cash by issuing to investors beneficial interests that pass through all cash received from the financial assets, and the transferor has no further involvement with the trust or the transferred financial assets. The Board understands that those securitizations generally would be judged as having isolated the assets~~;~~ because, in the absence of any continuing involvement, there would be reasonable assurance that the transfer would be found to be a true sale at law that places the assets beyond the reach of the transferor, its consolidated affiliates (that are not entities designed to make remote the possibility that it would enter bankruptcy or other receivership) included in the financial statements being presented, and its creditors, even in bankruptcy or other receivership.

82. In other securitizations, a similar corporation transfers financial assets to a securitization entity ~~an SPE~~ in exchange for cash and beneficial interests in the transferred financial assets. That entity raises the cash by issuing to investors commercial paper that gives them a senior beneficial interest in cash received from the financial assets. The beneficial interests obtained ~~that continue to be held~~ by the transferring corporation represent a junior interest to be reduced by any credit losses on the financial assets in the entity~~trust~~. The senior beneficial ~~commercial paper~~ interests (commercial paper) are highly rated by credit rating agencies only if both (a) the credit enhancement from the junior interest is sufficient and (b) the transferor is highly rated. Depending on facts and circumstances, the Board understands that those "single-step" securitizations often would be judged in the United States as not having isolated the financial assets, because the nature of the continuing involvement may make it difficult to obtain reasonable assurance that the transfer would be found to be a true sale at law that places the financial assets beyond the reach of the transferor, its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements presented, and its creditors in U.S. bankruptcy (paragraph 113). If the transferor fell into bankruptcy and the transfer was found not to be a true sale at law, investors in the transferred financial assets might be subjected to an automatic stay that would delay payments due them, and they might have to share in bankruptcy expenses and suffer further losses if the transfer was recharacterized as a secured loan.

83. Still other securitizations use multiple ~~two~~ transfers intended to isolate transferred financial assets beyond the reach of the transferor, its consolidated affiliates (that are not entities designed to make remote the possibility that it would enter bankruptcy or other receivership) included in the financial statements presented, and its creditors, even in bankruptcy. For example, in ~~In those~~ "two-step" structures:

a. First, the corporation transfers a group of financial assets to a special-purpose corporation that, although wholly owned, is so designed that the possibility is remote that the transferor, its other consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented, or its creditors could reclaim the financial assets ~~is remote~~. This first transfer is designed to be judged to be a true sale at law, in part because the transferor does not provide "excessive" credit or yield protection to the special-purpose corporation, and the Board understands that transferred financial assets are likely to be judged beyond the reach of the transferor, its other consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented, or the transferor's creditors even in bankruptcy or other receivership.
b. Second, the special-purpose corporation transfers ~~the assets~~ a group of financial assets

to a trust or other legal vehicle with a sufficient increase in the credit or yield protection on the second transfer (provided by a transferor's junior beneficial interest ~~that continues to be held by the transferor~~ or other means) to merit the high credit rating sought by third-party investors who buy senior beneficial interests in the trust. Because of that aspect of its design, that second transfer might not be judged to be a true sale at law and, thus, the transferred financial assets could at least in theory be reached by a bankruptcy trustee for the special-purpose corporation.

c. However, the special-purpose corporation is designed to make remote the possibility that it would enter bankruptcy, either by itself or by substantive consolidation into a bankruptcy of its parent should that occur. For example, its charter forbids it from undertaking any other business or incurring any liabilities, so that there can be no creditors to petition to place it in bankruptcy. Furthermore, its dedication to a single purpose is intended to make it extremely unlikely, even if it somehow entered bankruptcy, that a receiver under the U.S. Bankruptcy Code could reclaim the transferred financial assets because it has no other assets to substitute for the transferred financial assets.

The Board understands that the "two-step" securitizations described above, taken as a whole, generally would be judged under present U.S. law as having isolated the financial assets beyond the reach of the transferor, its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements presented, and its creditors, even in bankruptcy or other receivership. However, each entity involved in a transfer must be evaluated under the applicable consolidation accounting guidance. Accordingly, a transferor could be required to consolidate the trust or other legal vehicle used in the second step of the securitization, notwithstanding the isolation analysis of the transfer.

84. The powers of receivers for entities not subject to the U.S. Bankruptcy Code (for example, banks subject to receivership by the FDIC) vary considerably, and therefore some receivers may be able to reach financial assets transferred under a particular arrangement and others may not. A securitization may isolate transferred financial assets from a transferor subject to such a receiver and its creditors even though it is accomplished by only one transfer directly to a securitization entity ~~an SPE~~ that issues beneficial interests to investors and the transferor provides credit or yield protection. For entities that are subject to other possible bankruptcy, conservatorship, or other receivership procedures in the United States or other jurisdictions, judgments about whether transferred financial assets have been isolated need to be made in relation to the powers of bankruptcy courts or trustees, conservators, or receivers in those jurisdictions.

xx. Paragraphs 85 and 86, and 87, as amended, and 88:

85. Many transfers of financial assets that involve transfers of a group of entire financial assets to an entity whose sole purpose is to engage in securitization or asset-backed financing activities ~~in securitizations~~ empower the transferor to reclaim assets subject to certain restrictions. Such a power is sometimes called a removal-of-accounts provision (ROAP). Whether a ROAP precludes sale accounting depends on whether the ROAP results in the transferor's maintaining effective control over ~~specific~~ transferred financial assets (paragraph~~s~~ 9(c)~~(2) and 51–54~~).

86. The following are examples of ROAPs that preclude transfers from being accounted for as sales:

a. An unconditional ROAP or repurchase agreement that allows the transferor to specify the financial assets that may be removed and that provides a more-than-trivial benefit to the transferor, because such a provision allows the transferor unilaterally to remove specific financial assets
b. A ROAP conditioned on a transferor's decision to exit some portion of its business that provides a more-than-trivial benefit to the transferor, because whether it can be triggered by canceling an affinity relationship, spinning off a business segment, or accepting a third party's bid to purchase a specified (for example, geographic) portion of the transferor's business, such a provision allows the transferor unilaterally to remove specific financial assets.

87. The following are examples of ROAPs that *do not* preclude transfers from being accounted for as sales:

a. A ROAP for random removal of excess financial assets, if the ROAP is sufficiently limited so that the transferor cannot remove specific transferred financial assets, for example, by limiting removals to the amount of the transferor's interests ~~that continue to be held by the transferor~~ and to one removal per month
b. A ROAP for defaulted receivables, because the removal would be allowed only after a third party's action (default) and could not be caused unilaterally by the transferor
c. A ROAP conditioned on a third-party cancellation, or expiration without renewal, of an affinity or private-label arrangement, because the removal would be allowed only after a third party's action (cancellation) or decision not to act (expiration) and could not be caused unilaterally by the transferor.

88. A ROAP that can be exercised only in response to a third party's action that has not yet occurred does not maintain the transferor's effective control over financial assets potentially subject to that ROAP. However, when a third party's action (such as default or cancellation) or decision not to act (expiration) occurs that allows removal of financial assets to be initiated solely by the transferor and that provides a more-than-trivial benefit to the transferor, the transferor must recognize any financial assets subject to the ROAP, whether the ROAP is exercised or not. If the ROAP is exercised, the financial assets are recognized because the transferor has reclaimed the financial assets. If the ROAP is not exercised, the financial assets subject to the ROAP are recognized because the transferor now can unilaterally cause the transferee entity ~~qualifying SPE~~ to return those specific financial assets and, therefore, the transferor once again has effective control over those transferred financial assets (paragraph 55).

yy. Paragraph 89:

Sales-type and direct financing receivables secured by leased equipment, referred to as gross investment in lease receivables, are made up of two components: minimum lease payments and residual values. Minimum lease payments are requirements for lessees to pay cash to lessors and meet the definition of a financial asset. Thus, transfers of minimum lease payments are subject to the requirements of this Statement. Residual values represent the lessor's estimate of the "salvage" value of the leased equipment at the end of the lease term and may be either guaranteed or unguaranteed; residual values meet the definition of financial assets *to the extent that they are guaranteed at the inception of the lease*. Thus, transfers of residual values guaranteed at inception also are subject to the requirements of this Statement. Unguaranteed residual values do not meet the definition of financial assets, nor do residual values guaranteed after inception, and transfers of them are not subject to the requirements of this Statement. Transfers of residual values not guaranteed at inception continue to be subject to Statement 13, as amended. Because residual values guaranteed at inception are financial assets, increases to their estimated value over the life of the related lease are recognized. Entities selling or securitizing lease financing receivables shall allocate the gross investment in receivables between minimum lease payments, residual values guaranteed at inception, and residual values not guaranteed at inception using the individual carrying amounts of those components at the date of transfer. Those entities also shall record a servicing asset or servicing liability in accordance with paragraphs 10, 11, and 13, if appropriate.

zz. Paragraph 90:

At the beginning of the second year in a 10-year sales-type lease, Company F transfers ~~sells~~ for $505 a nine-tenths participating interest in the minimum lease payments to an independent third party, and the transfer is accounted for as a sale.[21a] Company F ~~and~~ retains a one-tenth participating interest in the minimum lease payments and a 100 percent interest in the unguaranteed residual value of leased equipment, which is not subject to the requirements of this Statement as discussed in paragraph 89 because it is not a financial asset and, therefore, is excluded from the analysis of whether the transfer of the nine-tenths participating interest in the minimum lease payments meets the definition of a participating interest. The servicing asset has a fair value of zero because Company F ~~receives~~

~~no explicit compensation for servicing, but it~~ estimates that the ~~other~~ benefits of servicing are just adequate to compensate it for its servicing responsibilities ~~and hence initially records no servicing asset or liability~~. The carrying amounts and related gain computation are as follows:

Carrying Amounts		
Minimum lease payments		$ 540
Unearned income related to minimum lease payments		370
Gross investment in minimum lease payments		910
Unguaranteed residual value	$ 30	
Unearned income related to unguaranteed residual value	60	
Gross investment in unguaranteed residual value		90
Total gross investment in financing lease receivable		$ 1,000

Gain on Sale		
Cash received		$ 505
Nine-tenths of carrying amount of gross investment in minimum lease payments	$ 819	
Nine-tenths of carrying amount of unearned income related to minimum lease payments	333	
Net carrying amount of minimum lease payments sold		486
Gain on sale		$ 19

Journal Entry		
Cash	505	
Unearned income	333	
Lease receivable		819
Gain on sale		19
To record sale of nine-tenths of the minimum lease payments at the beginning of year 2		

[21a]See footnote 18a.

aaa. Paragraphs 92 and 93:

92. ~~In some securities lending transactions,~~ If the ~~criteria~~ conditions in paragraph 9 are met~~, including the effective control criterion in paragraph 9(c), and consideration other than beneficial interests in the transferred assets is received. Those~~ securities lending transactions shall be accounted for (a) by the transferor as a sale of the "loaned" securities for proceeds consisting of the cash "collateral"[22] and a forward repurchase commitment and (b) by the transferee as a purchase of the "borrowed" securities in exchange for the "collateral" and a forward resale commitment. During the term of that agreement, the transferor has surrendered control over the securities transferred and the transferee has obtained control over those securities with the ability to sell or transfer them at will. In that case, creditors of the transferor have a claim only to the "collateral" and the forward repurchase commitment.

93. However, many securities lending transactions are accompanied by an agreement that both entitles and obligates the transferor to repurchase or redeem the transferred financial assets before their maturity under which the transferor maintains effective control over those financial assets (paragraphs 47–49). Those transactions shall be accounted for as secured borrowings, in which cash (or securities that the holder is permitted by contract or custom to sell or repledge) received as "collateral" is considered the amount borrowed, the securities "loaned" are considered pledged as collateral against the cash borrowed and reclassified as set

forth in paragraph 15(a), and any "rebate" paid to the transferee of securities is interest on the cash the transferor is considered to have borrowed.

bbb. Paragraphs 97–100:

97. Repurchase agreements can be effected in a variety of ways. Some repurchase agreements are similar to securities lending transactions in that the transferee has the right to sell or repledge the securities to a third party during the term of the repurchase agreement. In other repurchase agreements, the transferee does not have the right to sell or repledge the securities during the term of the repurchase agreement. For example, in a tri-party repurchase agreement, the transferor transfers securities to an independent third-party custodian that holds the securities during the term of the repurchase agreement. Also, many repurchase agreements are for short terms, often overnight, or have indefinite terms that allow either party to terminate the arrangement on short notice. However, other repurchase agreements are for longer terms, sometimes until the maturity of the transferred financial asset. Some repurchase agreements call for repurchase of securities that need not be identical to the securities transferred.

98. If the ~~criteria~~ conditions in paragraph 9 are met~~, including the criterion in paragraph 9(c)(1)~~, the transferor shall account for the repurchase agreement as a sale of financial assets and a forward repurchase commitment, and the transferee shall account for the agreement as a purchase of financial assets and a forward resale commitment. Other transfers that are accompanied by an agreement to repurchase the transferred financial assets that may ~~shall~~ be accounted for as sales include transfers with agreements to repurchase at maturity and transfers with repurchase agreements in which the [transferor] has not obtained collateral sufficient to fund substantially all of the cost of purchasing replacement financial assets.

99. Furthermore, "wash sales" that previously were not recognized if the same financial asset was purchased soon before or after the sale shall be accounted for as sales under this Statement. Unless there is a concurrent contract to repurchase or redeem the transferred financial assets from the transferee, the transferor does not maintain effective control over the transferred financial assets.

100. As with securities lending transactions, under many agreements to repurchase transferred financial assets before their maturity the transferor maintains effective control over those financial assets. Repurchase agreements that do not meet all the ~~criteria~~ conditions in paragraph 9 shall be treated as secured borrowings. Fixed-coupon and dollar-roll repurchase agreements, and other contracts under which the securities to be repurchased need not be the same as the securities sold, qualify as borrowings if the return of substantially the same (paragraph 48) securities as those concurrently transferred is assured. Therefore, those transactions shall be accounted for as secured borrowings by both parties to the transfer.

ccc. Paragraph 103:

A loan syndication is not a transfer of financial assets. Each lender in the syndication shall account for the amounts it is owed by the borrower. Repayments by the borrower may be made to a lead lender that then distributes the collections to the other lenders of the syndicate. In those circumstances, the lead lender is simply functioning as a servicer and, therefore, shall not recognize the aggregate loan as a~~n~~ financial asset.

ddd. Paragraph 104:

Groups of banks or other entities also may jointly fund large borrowings through loan participations in which a single lender makes a large loan to a borrower and subsequently transfers ~~undivided~~ interests in the loan to other entities.

eee. Paragraph 106:

If the loan participation agreement transfers a participating interest in an entire financial asset (as described in paragraph 8B of this Statement) ~~gives the transferee the right to pledge or exchange those participations~~ and the ~~other criteria~~ conditions in paragraph 9 are met, the transfer~~s to the transferee~~ shall be accounted for by the transferor as a sale~~s~~ of a participating interest. ~~financial assets.~~ A transferor's right of first refusal on a bona fide offer from a third party, a requirement to obtain the transferor's permission that shall not be unreasonably withheld, or a prohibition on sale to the transferor's competitor if other potential willing buyers exist is a limitation on the transferee's rights but presumptively does not constrain a transferee from exercising its right to pledge or exchange. However, if the loan participation agreement constrains the transferee~~s~~ from pledging or exchanging ~~their participations~~its participating interest and that constraint provides a more-than-trivial benefit to the transferor~~, the transferor presumptively receives a more than trivial benefit~~, the transferor has not relinquished control ~~over the loan,~~ and shall account for the transfer~~s~~ as a secured borrowing~~s~~.

fff. Paragraph 112:

Factoring arrangements are a means of discounting accounts receivable on a nonrecourse, notification basis. Accounts receivable in their entireties are sold outright, usually to a transferee (the factor) that assumes the full risk of collection, without recourse to the transferor in the event of a loss. Debtors are directed to send payments to the transferee. Factoring arrangements that meet the ~~criteria~~ conditions in paragraph 9 shall be accounted for as sales of financial assets because the transferor surrenders control over the receivables to the factor.

ggg. Paragraph 113:

In a transfer of an entire receivable~~s~~, a group of entire receivables, or a portion of an entire receivable with recourse, the transferor provides the transferee with full or limited recourse. A transfer of a portion of a receivable with recourse does not meet the requirements of a participating interest and shall be accounted for as a secured borrowing. The transferor is obligated under the terms of the recourse provision to make payments to the transferee or to repurchase receivables sold under certain circumstances, typically for defaults up to a specified percentage. The effect of a recourse provision on the application of paragraph 9 may vary by jurisdiction. In some jurisdictions, transfers with full recourse may not place transferred financial assets beyond the reach of the transferor, its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented, and its creditors, but transfers with limited recourse may. A transfer of receivables in their entireties with recourse shall be accounted for as a sale, with the proceeds of the sale reduced by the fair value of the recourse obligation, if the ~~criteria~~ conditions in paragraph 9 are met. Otherwise, a transfer of receivables with recourse shall be accounted for as a secured borrowing.

hhh. Appendix C, "Illustrative Guidance," paragraphs 342–349A, is deleted.

iii. Paragraph 364 (glossary), as amended:

[For ease of use, only those terms that are affected by this Statement have been reproduced.]

Beneficial interests

Rights to receive all or portions of specified cash inflows ~~to~~ received by a trust or other entity, including, but not limited to, senior and subordinated shares of interest, principal, or other cash inflows to be "passed-through" or "paid-through," premiums due to guarantors, commercial paper obligations, and residual interests, whether in the form of debt or equity.

Cleanup call

An option held by the servicer or its affiliate, which may be the transferor, to purchase the remaining transferred financial assets, or the remaining beneficial interests not held by the transferor, its affiliates, or its agents in an ~~qualifying SPE~~ entity (or in a series of beneficial interests in transferred financial assets within an ~~qualifying SPE~~ entity), if the amount of outstanding financial assets or beneficial interests falls to a level at which the cost of servicing those assets or beneficial interests becomes burdensome in relation to the benefits of servicing.

Consolidated affiliate ~~of the transferor~~

An entity whose assets and liabilities are included with those of the transferor in the consolidated, combined, or other financial statements being presented.

Continuing involvement

Any involvement with the transferred financial assets that permits the transferor to receive cash flows or other benefits that arise from the transferred financial assets or that obligates the transferor to provide additional cash flows or other assets to any party related to the transfer. All available evidence shall be considered, including, but not limited to, explicit written arrangements, communications between the transferor and the transferee or its beneficial interest holders, and unwritten arrangements customary in similar transfers. Examples of continuing involvement with the transferred financial assets include, but are not limited to, servicing arrangements, recourse or guarantee arrangements, agreements to purchase or redeem transferred financial assets, options written or held, derivative financial instruments that are entered into contemporaneously with, or in contemplation of, the transfer, arrangements to provide financial support, pledges of collateral, and the transferor's beneficial interests in the transferred financial assets.

Contractually specified servicing fees

All amounts that, per contract, are due to the servicer in exchange for servicing the financial asset and would no longer be received by a servicer if the beneficial owners of the serviced assets (or their trustees or agents) were to exercise their actual or potential authority under the contract to shift the servicing to another servicer. Depending on the servicing contract, those fees may include some or all of the difference between the interest rate collectible on the financial asset being serviced and the rate to be paid to the beneficial owners of those financial assets.

Financial asset

Cash, evidence of an ownership interest in an entity, or a contract that conveys to [one] entity a right (a) to receive cash or another financial instrument from a [second] entity or (b) to exchange other financial instruments on potentially favorable terms with the [second] entity.

Financial liability

A contract that imposes on one entity [an] obligation (a) to deliver cash or another financial instrument to a second entity or (b) to exchange other financial instruments on potentially unfavorable terms with the second entity.

~~**Guaranteed mortgage securitization**~~

~~A securitization of mortgage loans that is within the scope of FASB Statement No. 65, *Accounting for Certain Mortgage Banking Activities,* as amended, and includes a substantive guarantee by a third party.~~

Participating interest

A participating interest has the following characteristics:

a. From the date of the transfer, it represents a proportionate (pro rata) ownership interest in an entire financial asset. The percentage of ownership interests held by the transferor in the entire financial asset may vary over time, while the entire financial asset remains outstanding as long as the resulting portions held by the transferor (including any participating interest retained by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents) and the transferee(s) meet the other characteristics of a participating interest. For example, if the transferor's interest in an entire financial asset changes because it subsequently sells another interest in the entire financial asset, the interest held initially and subsequently by the transferor must meet the definition of a participating interest.
b. From the date of the transfer, all cash flows received from the entire financial asset are divided proportionately among the participating interest holders in an amount equal to their share of ownership. Cash flows allocated as compensation for services performed, if any, shall not be included in that determination provided those cash flows are not subordinate to the proportionate cash flows of the participating interest and are not significantly above an amount that would fairly compensate a substitute service provider, should one be required, which includes the profit that would be demanded in the marketplace. In addition, any cash flows received by the transferor as proceeds of the transfer of the participating interest shall be excluded from the determination of proportionate cash flows provided that the transfer does not result in the transferor receiving an ownership interest in

the financial asset that permits it to receive disproportionate cash flows.

c. The rights of each participating interest holder (including the transferor in its role as a participating interest holder) have the same priority, and no participating interest holder's interest is subordinated to the interest of another participating interest holder. That priority does not change in the event of bankruptcy or other receivership of the transferor, the original debtor, or any other participating interest holder. Participating interest holders have no recourse to the transferor (or its consolidated affiliates included in the financial statements being presented or its agents) or to each other, other than standard representations and warranties, ongoing contractual obligations to service the entire financial asset and administer the transfer contract, and contractual obligations to share in any set-off benefits received by any participating interest holder. That is, no participating interest holder is entitled to receive cash before any other participating interest holder under its contractual rights as a participating interest holder. For example, if a participating interest holder also is the servicer of the entire financial asset and receives cash in its role as servicer, that arrangement would not violate this requirement.

d. No party has the right to pledge or exchange the entire financial asset unless all participating interest holders agree to pledge or exchange the entire financial asset.

Proceeds

Cash, beneficial interests, servicing assets, derivatives, or other assets that are obtained in a transfer of financial assets, less any liabilities incurred.

Standard representations and warranties

Representations and warranties that assert the financial asset being transferred is what it is purported to be at the transfer date. Examples include representations and warranties about (a) the characteristics, nature, and quality of the underlying financial asset, including characteristics of the underlying borrower and the type and nature of the collateral securing the underlying financial asset, (b) the quality, accuracy, and delivery of documentation relating to the transfer and the underlying financial asset, and (c) the accuracy of the transferor's representations in relation to the underlying financial asset.

Transferee

An entity that receives a financial asset, an interest in ~~a portion of~~ a financial asset, or a group of financial assets from a transferor.

Transferor

An entity that transfers a financial asset, an interest in ~~a portion of~~ a financial asset, or a group of financial assets that it controls to another entity.

~~**Undivided interest**~~

~~Partial legal or beneficial ownership of an asset as a tenant in common with others. The proportion owned may be pro rata, for example, the right to receive 50 percent of all cash flows from a security, or non–pro rata, for example, the right to receive the interest from a security while another has the right to the principal.~~

EFFECTIVE DATE AND TRANSITION

5. This Statement shall be effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. Earlier application is prohibited. The recognition and measurement provisions of this Statement shall be applied to transfers that occur on or after the effective date.

6. Additionally, on and after the effective date, existing qualifying special-purpose entities (as defined under previous accounting standards) must be evaluated for consolidation by reporting entities in accordance with the applicable consolidation guidance. If the evaluation on the effective date results in consolidation, the reporting entity shall apply the transition guidance provided in the pronouncement that requires consolidation.

7. The disclosure provisions of this Statement shall be applied to transfers that occurred both before and after the effective date of this Statement. An entity is encouraged, but not required, to disclose comparative

information for periods earlier than the effective date for disclosures that were not previously required by Statement 140 for nonpublic entities or by FASB Staff Position FAS 140-4 and FIN 46(R)-8, *Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities,* for public entities. Comparative disclosures for those disclosures that were not previously required by Statement 140 for nonpublic entities or by FSP FAS 140-4 and FIN 46(R)-8 for public entities are required only for periods after the effective date.

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

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

Robert H. Herz, *Chairman*	Thomas J. Linsmeier	Marc A. Siegel
	Leslie F. Seidman	Lawrence W. Smith

Appendix A

BACKGROUND INFORMATION AND BASIS FOR CONCLUSIONS

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Appendix A

BACKGROUND INFORMATION AND BASIS FOR CONCLUSIONS

Introduction and Background

A1. This appendix summarizes considerations that Board members deemed significant in reaching the conclusions in this Statement. This appendix explains the Board's reasons for accepting certain views and rejecting others in deciding to remove the concept of a qualifying special-purpose entity from FASB Statement No. 140*, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* and to amend other provisions in that Statement. Individual Board members gave greater weight to some factors than to others.

A2. The Board decided to undertake a project on the permitted activities of qualifying special-purpose entities in 2003 for two main reasons. First, Statement 140, which was issued in September 2000 as a replacement of FASB Statement No. 125, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* established conditions that an entity must meet to be a qualifying special-purpose entity. However, Statement 140 did not specify the powers of a qualifying special-purpose entity required to retire and reissue beneficial interests. In 2002, the Emerging Issues Task Force (EITF) attempted to clarify those powers but did not reach a consensus. That effort was designated as EITF Issue No. 02-12, "Permitted Activities of a Qualifying Special-Purpose Entity in Issuing Beneficial Interests under FASB Statement No. 140." Second, FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities,* did not apply to interests in qualifying special-purpose entities, except in certain limited circumstances. Because a qualifying special-purpose entity generally was exempt from consolidation, the Board decided that it was important to clarify its characteristics.

A3. In June 2003, the Board issued the Exposure Draft, *Qualifying Special-Purpose Entities and Isolation of Transferred Assets,* and received 52 comment letters in response to that Exposure Draft. In August 2003, 26 participants discussed their views with the Board at a public roundtable meeting. Following that meeting, the Board met in a series of public meetings to redeliberate the issues and to consider the concerns raised by respondents in comment letters and at the roundtable meeting. During the redeliberations of that Exposure Draft, the Board expanded the scope of the project to clarify how to apply the derecognition guidance to a transfer of a portion of a financial asset, to clarify and improve the guidance on isolation, and to improve the guidance on the initial measurement of a transferor's interest in a transferred financial asset.

A4. In its redeliberations of the 2003 Exposure Draft, the Board decided that additional information about isolation issues was necessary, including how set-off rights between an original borrower and a transferor affect the isolation analysis. In April 2004, the staff posted for public comment an FASB Staff Request for Information about the isolation of transferred financial assets and set-off rights and received 33 comment letters in response. The Board held two public roundtable meetings in May and June 2004 to improve its understanding of the factors that attorneys consider in rendering an opinion on the legal status of transfers of financial assets.

A5. Because the conclusions reached during redeliberations were substantially different from the conclusions in the 2003 Exposure Draft on qualifying special-purpose entities and isolation of transferred financial assets, the Board decided it needed additional input from constituents. Thus, the Board issued a revised Exposure Draft, *Accounting for Transfers of Financial Assets,* in August 2005. The Board received 57 comment letters in response to that Exposure Draft and continued to redeliberate the issues in a series of public meetings.

A6. After the issuance of the 2005 Exposure Draft, the Board continued to receive questions about the permitted activities of a qualifying special-purpose entity, including requests from constituents to address questions about qualifying special-purpose entities used in commercial and residential mortgage loan securitizations. Constituents also asked whether the status of a qualifying special-purpose entity could be retained if the underlying loans were modified before an event of default. During redeliberations, financial statement users and other constituents asserted that many derecognized financial assets should continue to be reported by transferors in their statements of financial position. Many financial statement users told the Board that they routinely add derecognized financial assets back to the statement of financial position when performing economic analyses of a transferor's financial statements. Many users also told the Board that sale accounting should not be permitted if a transferor has any continuing involvement in the transferred financial assets.

A7. In September 2008, the Board issued a third Exposure Draft, *Accounting for Transfers of Financial Assets,* that proposed, among other things, to (a) eliminate the concept of a qualifying special-purpose entity and the related exception from consolidation for qualifying special-purpose entities, (b) modify the financial-components approach used in Statement 140, (c) strengthen and clarify the derecognition conditions in paragraph 9 of Statement 140, and (d) improve the disclosure requirements for transferred financial assets. The Board simultaneously issued an Exposure Draft, *Amendments to FASB Interpretation No. 46(R),* in a separate, but related project that proposed amendments to the consolidation guidance in Interpretation 46(R). The Board undertook that project due, in part, to the proposed elimination of the concept of a qualifying special-purpose entity and the expectation that many securitization entities previously exempt from Interpretation 46(R) would become subject to its provisions.

A8. The Board received 51 comment letters on the 2008 Exposure Draft on accounting for transfers of financial assets. The Board held two public roundtable meetings in November 2008 to discuss constituent views on the 2008 Exposure Drafts on accounting for transfers of financial assets and amendments to Interpretation 46(R). This Statement is the result of deliberations on the feedback received on the 2005 and 2008 Exposure Drafts on accounting for transfers of financial assets, continued constituent inquiries (including financial statement user requests for greater transparency), and market conditions over recent years including, but not limited to, the impact of the recent credit crisis.

A9. Since 2003, the Board has issued two Statements and four FSPs that amend particular aspects of Statement 140. The Board issued FASB Statements No. 155, *Accounting for Certain Hybrid Financial Instruments,* and No. 156, *Accounting for Servicing of Financial Assets,* and FSP FAS 140-1, *Accounting for Accrued Interest Receivable Related to Securitized and Sold Receivables under FASB Statement No. 140,* FSP FAS 140-2, *Clarification of the Application of Paragraphs 40(b) and 40(c) of FASB Statement No. 140,* and FSP FAS 140-3, *Accounting for Transfers of Financial Assets and Repurchase Financing Transactions.*

A10. In December 2008, the Board issued FSP FAS 140-4 and FIN 46(R)-8, *Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities.* That disclosure-only FSP incorporates many of the proposed disclosure requirements included in the 2008 Exposure Drafts on accounting for transfers of financial assets and amendments to Interpretation 46(R). During the Board deliberations of the 2008 Exposure Drafts, the Board decided to issue separately the disclosure-only FSP to expeditiously meet financial statement user needs for greater transparency of off-balance-sheet transactions and to provide adequate time for preparers and others to consider and implement the other amendments to Statement 140 and Interpretation 46(R). FSP FAS 140-4 and FIN-46(R)-8 was effective for public entities for the first reporting period (interim or annual) ending after December 15, 2008. This Statement, along with FASB Statement No. 167, *Amendments to FASB Interpretation No. 46(R),* supersedes that disclosure-only FSP and carries forward most of the incremental Statement 140-related disclosures from that FSP.

Amendments and Modifications to Statement 140

A11. Many financial statement users recommended that the Board adopt a no-continuing-involvement model as an alternative to the financial-components approach in Statement 140. As discussed in paragraph A6, those users stated that derecognition should not be permitted if a transferor has any continuing involvement in the transferred financial assets with the exception of fiduciary servicing. Many users told the Board that they disagree with the financial-components approach because it permits derecognition of components of a financial asset or a pool of financial assets when the transferor remains in control of the underlying financial asset(s) through its continuing involvement with the transferred financial asset(s). Some financial statement users stated that there should be a rebuttable presumption that a transferor maintains effective control over transferred financial assets when it has continuing involvement with the original financial assets.

A12. Other constituents stated that a no-continuing-involvement model would be a significant change from the financial-components approach that is the fundamental basis for Statement 140. Those constituents noted that a no-continuing-involvement model would be inconsistent with the Board's stated objective that the amendments to Statement 140 in this

Statement are intended to provide a short-term solution to address inconsistencies in practice in the context of the existing concepts in Statement 140 until such time as convergent standards on derecognition and consolidation are developed with the International Accounting Standards Board (IASB). They noted that a no-continuing-involvement model would be inconsistent with the 2009 IASB Exposure Draft, *Derecognition.* Constituents also stated that a no-continuing-involvement model would not properly reflect the underlying economics of many transfers and that a financial-components approach would better reflect the economics of many transfers. For example, they stated that for a no-continuing-involvement model to be operational, exceptions would be required to the general principle of no continuing involvement. They also noted that certain financial statement users would permit an exception for fiduciary servicing. These constituents stated that servicing is broad and that defining fiduciary servicing will likely be difficult, as evidenced by the Board's deliberations on servicer discretion (see paragraphs A29 and A30).

A13. To address the concerns of financial statement users and other constituents, the Board decided to (a) reevaluate the financial-components approach, (b) define when it is appropriate to derecognize a portion of an entire financial asset, and (c) reevaluate the conditions for sale accounting described in paragraph 9 of Statement 140. The Board also decided to clarify the guidance about the types of continuing involvement that (1) indicate that a transferor continues to control transferred financial assets and (2) do not indicate that a transferor continues to control transferred financial assets. In addition, the Board decided to enhance the disclosure requirements about a transferor's continuing involvement with transferred financial assets.

Control of Portions of Financial Assets

A14. In developing Statement 140 and its predecessor, Statement 125, the Board adopted a financial-components approach for sale accounting that is based on the concept that each party to a transfer of financial assets recognizes the assets and liabilities that it controls after the transfer. The financial-components approach analyzes a transfer of a financial asset by examining the component assets (controlled economic benefits) and liabilities (obligations for probable future sacrifices of economic benefits) that exist after the transfer. Each party to the transfer recognizes the assets that it controls and the liabilities that it assumes as a result of the transfer and no longer recognizes the assets and liabilities that were surrendered or extinguished in the transfer. The Board concluded that one of the keys to the financial-components approach is that a transferor should no longer recognize a transferred financial asset if it has surrendered control of the asset. The Board provided guidance on the conditions that must be met for a transferor to be deemed to have surrendered control over transferred financial assets (or all or a portion of a financial asset) as described in paragraph 9 of Statement 140. However, the Board did not provide explicit guidance on what constitutes a portion or a component of a financial asset.

A15. After Statement 140 was issued, auditors, regulators, and other constituents raised concerns about certain transfers of portions of a financial asset that were being accounted for as sales. In particular, constituents raised concerns about certain sales of undivided interests in pools of financial assets because of significant credit support provided by affiliates of the transferors. The constituents indicated that, in some cases, transferred financial assets appear to have remained under the control of the transferor while being reported as sales. Constituents and regulators also expressed concerns about highly structured transactions that were treated as sales when, in their view, the transferor continued to control the transferred financial assets, as evidenced by the fact that the underlying financial assets continued to be in the custody of the transferor and/or its consolidated affiliates and the transferor had significant continuing involvement through its interests in the underlying financial asset(s).

A16. In its 2005 Exposure Draft, the Board concluded that, in practice, it is difficult to determine whether a transferor has surrendered control over a component of a financial asset, or a component of a group of financial assets, if the transferor continues to maintain custody of the original financial asset(s). Therefore, the Board decided to limit sale accounting to transfers of entire financial assets, or a group of entire financial assets, unless the transferred portion mirrors the characteristics of the original financial asset. The Board established the definition of a *participating interest* to describe when it is appropriate to evaluate a transferred portion of a financial asset for sale accounting. In developing that guidance, the Board considered the requests of financial statement users for a no-continuing-involvement model. The Board decided that it was only appropriate to apply the sale accounting conditions to a portion of a financial asset if the transferor and transferee proportionately share in all of the rights, risks, and benefits of the entire financial asset.

A17. During its deliberations of the 2008 Exposure Draft on accounting for transfers of financial assets, the Board considered constituents' comments about participating interests and decided to reaffirm its decision to use the definition of a participating interest to limit the circumstances when it is appropriate to evaluate a transfer of a portion of a financial asset for sale accounting. In reaffirming its decision, the Board determined that it was necessary to provide specific guidance on the definition of a portion of a financial asset that is eligible for sale accounting.

A18. This Statement added paragraph 8B to Statement 140 to establish the unit of account to which the sale accounting conditions in paragraph 9 of Statement 140, as amended by this Statement, must be applied to transfers of financial assets. Paragraph 8B states that paragraph 9 should be applied to transfers of an entire financial asset, transfers of a group of entire financial assets, and transfers of a participating interest in an entire financial asset. Inherent in that principle is that to be eligible for sale accounting, an entire financial asset cannot be divided into components before the transfer unless those components meet the definition of a participating interest. As a result, this Statement modifies the financial-components approach to limit the circumstances for sale accounting by requiring that the conditions in paragraph 9 for surrender of control be applied only to a transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset. However, this Statement retains certain of the concepts in the financial-components approach in that a transferor continues to recognize assets obtained and liabilities incurred in a transfer of financial assets accounted for as a sale. In a transfer of an entire financial asset or a group of entire financial assets, the assets obtained may include a beneficial interest in a transferred financial asset that is similar to a component, but only if a transferor transfers and surrenders control over the entire original financial asset or the group of entire financial assets. In other words, this Statement permits a transferor to obtain a beneficial interest in the transferred financial asset as proceeds from the transfer if it has surrendered control over the original financial asset in a transfer to an unconsolidated entity that meets all of the conditions in paragraph 9 of Statement 140, as amended by this Statement.

Characteristics of participating interests

A19. In developing the definition of a participating interest in the 2005 and 2008 Exposure Drafts, the Board considered the conditions in IAS 39, *Financial Instruments,* for applying the derecognition conditions for transferred portions of a financial asset. The participating interest definition is similar to the conditions in IAS 39 for transfers of portions of financial assets; however, IAS 39 also permits portions that represent specifically identified cash flows in individual financial assets or groups of similar financial assets to be evaluated for derecognition. During its deliberations of the 2005 and 2008 Exposure Drafts, the Board decided not to adopt the guidance for portions of financial assets in IAS 39 because the Board was concerned that certain apportionments permitted in IAS 39 would lead to subordination. For example, in the transfer of a five-year loan in which payments in the first five years would be interest-only payments and the entire principal would be due at the end of five years as a balloon payment, IAS 39 would permit derecognition for the interest-only payments even if the transferor retained rights to the entire principal portion of the loan. The Board concluded that such an arrangement has a similar effect as that in a subordination arrangement because the early cash flows would all go to one interest holder with the latter, more risky payments going to another interest holder.

A20. Some respondents to the 2005 and 2008 Exposure Drafts asked the Board to clarify the definition of a participating interest, which it has done in this Statement. Respondents to the 2005 Exposure Draft commented that the prohibition on recourse in the participating interest definition inappropriately included standard representations and warranties. The 2008 Exposure Draft excluded standard representations and warranties; however, respondents to that Exposure Draft told the Board that a transferor may have other contractual obligations in its role as servicer that could result in the transferee having recourse to the transferor. In its redeliberations, the Board decided to specifically exclude recourse related to the transferor's ongoing contractual obligations to service the financial assets and administer the transfer contract. In developing the participating interest definition, the Board was concerned about a transferor providing financial support to a transferee, but the Board does not believe that standard representations and warranties result in the transferor providing financial support to the transferee.

A21. Respondents to the 2008 Exposure Draft asked the Board to clarify whether a third-party guarantee received by a transferor that is passed on to other interest holders would affect the determination of whether a transferred portion of a financial asset meets the definition of a participating interest. Some respondents noted that in certain transfers the transferor retains the unguaranteed portion but transfers a portion along with a guarantee provided by a third party to those interest holders. The Board decided that third-party guarantees should not affect whether the participating interest definition is met. The Board reasoned that an independent third-party guarantee is an arrangement in which a third-party guarantor would assume a participating interest in the event of default that does not result in recourse to the transferor or to other participating interest holders. As a result, the Board concluded that third-party guarantees should be excluded from the evaluation of whether the participating interest definition is met.

A22. Some respondents to the 2008 Exposure Draft stated that cash flows received that represent the transferor's gain or loss on the sale should be specifically excluded from the determination of whether cash flows are proportionate. Those respondents noted that a participating interest may be transferred after the purchase or origination of the financial asset. Often the interest rate passed through to the transferee for the portion of the asset transferred is based on the market rate at the time of transfer and differs from the contractual interest rate on the financial asset. Respondents noted that under the 2008 Exposure Draft, the transferor would need to either (a) transfer the participating interest at a premium, in which case the transferee would pay the transferor upfront, or (b) incorporate the excess interest into the servicing fee, in which case the gain or loss resulting from changes in market rates would be recognized over time through the conveyance of an interest-only strip to the transferor from the transferee. The Board was concerned with incorporating the excess interest into the servicing fee because it would result in the transferor retaining prepayment risk related to the transferred portion of the financial asset. Furthermore, the Board noted that an interest-only strip received as proceeds would not meet the definition of a participating interest. As a result, the Board decided that the concept of a participating interest is consistently applied only when a premium, if any, is not dependent on the cash flows from the transferred participating interest. The Board decided that a transferor cannot receive an interest-only strip as proceeds from a transfer of a participating interest because the future cash flows would not be proportionately shared by all participating interest holders.

A23. The Board recognizes that Statement 140 used the term *undivided interest* inconsistently and that many constituents considered that term to be synonymous with the phrase *portion of a financial asset* for purposes of applying the conditions for sale accounting in paragraph 9 of Statement 140. To eliminate the inconsistent use of the term *undivided interest,* the Board decided to delete the term *undivided interest* from this Statement.

Amendments Related to Qualifying Special-Purpose Entities

A24. The Board concluded in Statement 125, and reaffirmed in Statement 140, that if there is a transfer of financial assets to a qualifying special-purpose entity that cannot pledge or exchange the transferred financial assets, the transferor should nevertheless generally be permitted to derecognize the transferred financial assets if (a) the holders of interests issued by that entity could pledge or exchange their interests and (b) the transfer meets the other conditions for sale accounting in Statement 140. Accordingly, the Board developed conditions for a qualifying special-purpose entity to ensure that consideration for consolidation would not be pertinent because the entity would be so passive that control could not be an issue. Consequently, paragraph 46 of Statement 140 exempts a qualifying special-purpose entity from consolidation because (1) its primary purpose is limited to passively holding financial assets on behalf of its beneficial interest holders and (2) the Board's understanding was that no individual party would have the ability to control such an entity. The Board generally excluded qualifying special-purpose entities from the scope of Interpretation 46(R) for the same reasons.

A25. When it developed the conditions for qualifying special-purpose entities in Statements 125 and 140, the Board believed that transferee entities used in securitizations were passive pass-through entities that received a pool of financial instruments and concurrently issued beneficial interests. The Board has learned that, in practice, the conditions specified in paragraph 35(b) of Statement 140 that require a qualifying special-purpose entity's activities to be *significantly limited* and *entirely specified* were being applied more broadly than originally intended in many securitizations that were being reported as sales. The following are some of the issues that raised questions about whether the passivity conditions required for a qualifying special-purpose entity were met and enforced in practice:

a. Rollovers of beneficial interests
b. Servicer discretion
c. Constituent and Securities and Exchange Commission (SEC) staff inquiries about whether a qualifying special-purpose entity could maintain its qualifying status when responding to unexpected events, such as the need to modify loans to reduce the risk of default.

As a result, the Board decided to remove the concept of a qualifying special-purpose entity in its entirety from this Statement.

Rollovers of beneficial interests

A26. The Board began this project because of questions raised about whether the restrictive conditions for a qualifying special-purpose entity, which require the terms of beneficial interests to be specified at inception of the entity, can be met if a qualifying special-purpose entity (or its designee or agent) is permitted to establish the terms of replacement beneficial interests issued after inception of the qualifying special-purpose entity. The Board also questioned whether an existing qualifying special-purpose entity (or its designee or agent) that determines the terms of beneficial interests issued after the inception of the qualifying special-purpose entity satisfies the passivity requirements in Statement 140.

A27. The Board learned that qualifying special-purpose entities often finance long-term financial assets by issuing short-term beneficial interests in the form of commercial paper or other debt instruments that, in the aggregate, do not receive all the cash inflows from the pool of assets. When those initial beneficial interests mature, they are paid off from the proceeds from issuing new beneficial interests, rather than from the cash inflows from the pool of financial assets. Frequently, such entities are supported by liquidity commitments from the transferor or other parties to ensure that the obligations of the entity to redeem beneficial interests are met on a timely basis. The Board questioned whether the combination of an entity's ability to make decisions about future refinancing and the involvement of a liquidity provider would be inconsistent with the requirements that the activities of a qualifying special-purpose entity be significantly limited and entirely specified. The Board also questioned whether such discretion and involvement effectively enable a transferor or servicer to establish a controlling financial interest in an entity (as described in Interpretation 46(R)) and, furthermore, whether a qualifying special-purpose entity should continue to be generally excluded from the scope of Interpretation 46(R) and other consolidation guidance.

A28. In the 2005 Exposure Draft, the Board decided to address the issue of rollovers by specifying that no party may have two or more involvements with a qualifying special-purpose entity that provide that party with the opportunity to obtain a more-than-trivial benefit relative to the benefit that would be obtained if separate parties had those same involvements. Respondents to that Exposure Draft generally objected to the proposed amendment, principally because they said it could not be operationalized without extensive additional guidance and would be difficult to audit.

Servicer discretion

A29. Members of the largest accounting firms and representatives of the commercial and residential mortgage securitization industry raised questions about the amount of discretion a servicer is permitted in servicing the financial assets of a qualifying special-purpose entity. They asked for clarification of the requirement that the activities of a qualifying special-purpose entity be significantly limited and entirely specified in the legal documents that establish the qualifying special-purpose entity or that create the beneficial interests in the transferred financial assets. It was noted that in most securitization transactions, it may not be commercially feasible to describe every event that may occur or to identify an automatic response to every event. The issues that were raised focused on whether certain types of entities met the conditions of a qualifying special-purpose entity and on how much discretion a servicer of a qualifying special-purpose entity should be allowed when responding to events outside the control of the transferor.

A30. The staff and some Board members met with constituents and concluded that, in practice, many qualifying special-purpose entities hold financial assets that do not appear to be passive in nature. In addition, many entities require a servicer to exercise a level of decision making that does not appear to have been entirely prespecified if unforeseen events occur or to engage in activities that reach beyond the requirement in Statement 140 that the activities of a qualifying special-purpose entity be significantly limited. Some parties indicated that the long-term nature of many of these transactions makes it impractical to predict all of the possible events that may occur during the life of the transferred financial asset. In addition, it is impractical for the same reason to predict all of the potential responses a servicer might be required to make to protect the interests of the beneficial interest holders. Consequently, the Board concluded that it would not be feasible or fruitful to define at inception the parameters required by the definition of a qualifying special-purpose entity for many types of financial assets, most notably financial assets with longer terms.

Loan modifications

A31. In June 2007, the FASB staff hosted an educational forum to gather information about the legal, tax, accounting, and regulatory consequences of proposed modifications to certain securitized residential mortgage loans, such as subprime loans. The forum was designed to determine whether regulators or accounting standard setters needed to provide additional guidance. It engaged a wide range of experts in a discussion of issues encountered by industry participants on modifications of securitized mortgage loans held in qualifying special-purpose entities. Discussions at the forum focused on the following issues:

a. Legal, tax, and regulatory constraints placed on securitization trusts in practice and the ramifications, or potential ramifications, of those constraints on the ability of a qualifying special-purpose entity to modify securitized mortgage loans
b. Views of preparers, financial statement users, auditors, and others on the accounting consequences of modifications to securitized mortgage loans.

A32. The proposed loan modifications at issue included those that were being made, or were planned to be made, in light of a statement from the federal financial institutions' regulatory agencies encouraging financial institutions to work constructively with residential borrowers who were financially unable to make their contractual payments on their home loans. Many of those modifications were proposed for loans that were not in default but for which an event of default appeared to be imminent or reasonably foreseeable. Some participants asserted that Statement 140 and related interpretive guidance are ambiguous about when an entity may modify a loan without affecting qualifying special-purpose entity status because the interpretive guidance states only that a servicer is permitted to work out a loan if it becomes delinquent or is in default. The guidance also requires that the discretion inherent in that decision be significantly limited and its parameters be entirely specified in the qualifying special-purpose entity's legal documents. Following the forum, the Board decided to consider that issue as part of its ongoing project on Statement 140.

Removal of the qualifying special-purpose entity concept

A33. The Board believes that because of the range of financial assets being securitized and the complexity of securitization structures and arrangements, the application of the conditions for a qualifying special-purpose entity have been extended in some cases beyond the intent of Statement 140, thus effectively rendering the conditions no longer operational in practice. The Board considered an approach that would have strengthened the passivity requirement of the permitted assets of a qualifying special-purpose entity; however, after discussing this possible approach with constituents, the Board concluded that few classes of financial assets are truly passive as envisioned in the qualifying special-purpose entity concept. As a result, the Board decided to remove the concept of a qualifying special-purpose entity from Statement 140.

A34. As a result of its decision to remove the concept of the qualifying special-purpose entity from Statement 140, the Board decided to remove the scope exception for qualifying special-purpose entities from consolidation guidance, including the guidance in Interpretation 46(R). The Board considered how eliminating the qualifying special-purpose entity concept could potentially affect the application of Interpretation 46(R) to formerly qualifying special-purpose entities and noted that the elimination would put additional pressure on the framework of that existing consolidation model. As a result of these and other concerns, the Board decided to add a separate but related project to reconsider the guidance in Interpretation 46(R).

Amendments Related to the Isolation of Transferred Financial Assets

A35. The Board decided it was necessary to simplify and clarify the isolation guidance in paragraph 9(a) of Statement 140 to improve comparability and consistency in the application of that guidance and related implementation guidance.

A36. Paragraph 27 of Statement 140 includes a requirement that, except for certain bankruptcy-remote entities, transferred financial assets must be isolated from any entities in the transferor's consolidated group. However, because of questions about the requirements and inconsistencies in practice, the Board decided to clarify the requirements for isolation. Consequently, the Board decided to amend paragraph 9(a) of Statement 140 to include language similar to that of paragraph 27 of Statement 140.

A37. In developing Statements 125 and 140, the Board concluded that the isolation condition is an important consideration in deciding whether to derecognize a financial asset. The Board acknowledged that a transferor would likely need to rely on a legal analysis of what would happen if the transferor enters bankruptcy or receivership. Several Board members observed that attorneys, including those who commented on the 2003 and 2005 Exposure Drafts on qualifying special-purpose entities and transfers of financial assets, do not always agree on whether a particular transaction meets the requirements for a true sale opinion. The nature of these opinions is described in paragraph 27A of Statement 140, as amended by this Statement. To provide a true sale opinion, an attorney must evaluate the facts and circumstances of a particular transaction and make a reasoned judgment about how a court would view the transferred financial assets on the basis of applicable statutory, common, and case laws that are relevant to the transaction. The Board is aware that attorneys may reach different conclusions about similar transactions because they may assess the facts and circumstances of a particular transaction differently or may interpret the law differently. During its redeliberations, the Board considered information (provided by attorneys, auditors, and regulators of financial institutions) describing the key characteristics that attorneys consider in rendering true sale and nonconsolidation opinions.

A38. The Board learned that for entities needing legal isolation under U.S. bankruptcy law, a true sale opinion and, in the case of transfers to affiliated entities, a nonconsolidation opinion often would be required by auditors to support a conclusion that a transferred financial asset had been isolated from the transferor, its consolidated affiliates included in the financial statements being presented, and its creditors. The Board also learned that in other jurisdictions an auditor often would require a true sale analysis, similar to a true sale opinion, to support a conclusion about whether a transferred financial asset has been isolated. The Board decided that it would not require a legal opinion for all transfers, because a transferor could sometimes determine through other means what the legal conclusion would be based on a transferor's experience with similar transfers. The Board acknowledged that the additional implementation guidance in paragraph 27A of Statement 140, as amended by this Statement, will be most helpful for transferors under the jurisdiction of U.S. bankruptcy law. However, the Board believes that the additional guidance will reduce practice issues for those transferors and provide an example that may be used by analogy by transferors under other legal jurisdictions.

A39. During its deliberations before issuing the 2005 Exposure Draft, the Board also considered the issue of set-off rights before concluding that the isolation requirement should continue to be based on a legal analysis. A set-off right is a common law right of a party that is both a debtor and a creditor to the same counterparty to reduce its obligation to that counterparty if that counterparty fails to pay its obligation. Attorneys at the roundtable meetings, respondents to the 2004 Staff Request for Information, and rating agencies told the Board that the existence of set-off rights is not considered by a court when assessing whether a transaction would be deemed to be a true sale. Attorneys told the Board that in the event of the bankruptcy or receivership of either the obligor of the financial asset or the transferor of the financial asset, both parties could retain the ability to exercise a set-off right involving a financial asset that had been transferred. In the event of the bankruptcy of the transferor, the transferee may have only an unsecured claim against the transferor for its share of the amount set off.

A40. Several Board members stated that set-off rights related to a transferred financial asset should be severed to meet the isolation requirement. However, the Board learned that it may not be possible to sever set-off rights related to transferred financial assets. For example, certain consumer protection rules prevent consumers from waiving their ability to exercise set-off rights against a seller of goods financed under a contract with the seller. In other cases, it may be impractical or infeasible for a transferor to sever set-off rights related to transferred financial assets because doing so would require the involvement of an obligor on the original financial assets who may not even be aware of or otherwise involved in the transfer. Attorneys told the Board that a court likely would compel a transferor that benefited from an exercise of set-off rights on a transferred financial asset to pass through a proportionate share of that benefit to any transferee that held a share of the related original financial asset. Constituents also told the Board that set-off risks are assessed and included in the price for the transaction like other dilutive risks, such as warranties and returns. The Board ultimately decided that set-off rights would not be an impediment to meeting the isolation requirement or the participating interest definition.

A41. Following the 2005 Exposure Draft, the Board considered but later rejected an alternative that would have required the isolation analysis to be performed on the basis of the legal consequences that would occur if all involvements of a transferor and any consolidated affiliates included in the financial statements being presented were attributed to the transferor as if the transferor had those involvements directly. The Board rejected that alternative because it believed the alternative would not reduce diversity in practice, but actually could increase diversity in practice, because it would require attorneys to make assumptions and decisions about hypothetical circumstances that would be unlikely to be tested in a court of law. However, the Board decided to clarify that the transferred financial assets must be placed beyond the reach of all consolidated affiliates, other than certain bankruptcy-remote entities, included in the financial statements being presented.

A42. The Board also discussed whether it would be more meaningful to provide an accounting definition of isolation that did not rely on a legal analysis. The Board rejected that proposal because it believes that the isolation principle is a fundamental cornerstone of Statement 140 that should be revised only in the context of a project to completely revisit the topic of derecognition. The Board decided that such a fundamental project should be conducted jointly with the IASB.

Amendments Related to Constraints on Transferability

A43. As noted above, the Board decided to eliminate the concept of a qualifying special-purpose entity and the exception for qualifying special-purpose entities in paragraph 9(b) of Statement 140. The Board then considered whether the transferee's ability to pledge or exchange the assets it receives should continue to be a condition for sale accounting. The Board concluded that the ability of a transferee to use the financial asset it receives is an important indication that a transferor has surrendered control over the transferred financial asset.

A44. In the 2008 Exposure Draft, the Board proposed that a constraint on the transferee's ability to pledge or exchange its assets indicates that a transferor maintains effective control over a transferred asset unless such a constraint is designed primarily to provide the transferee with a benefit. The Board decided that it was more appropriate to remove paragraph 9(b) from Statement 140 in its entirety and consider the effect of constraints on the transferee under paragraph 9(c), which addresses effective control. As a result, the Board included that guidance in paragraph 9(c)(3) of the 2008 Exposure Draft.

A45. Most of the respondents to the 2008 Exposure Draft stated that paragraph 9(c)(3) was not clear or operational or was overly subjective. The Board decided to retain the existing language in paragraph 9(b) with modification for the removal of the qualifying special-purpose entity concept. The Board decided to clarify when a transferor should look through to the third-party beneficial interest holders, rather than look to the transferee, in evaluating paragraph 9(b). The Board noted that certain transferees issue beneficial interests of various types—characterized as debt, participations, residual interests, or otherwise as required by the transfer agreements. To issue the beneficial interests, the transferee is typically restricted from pledging or exchanging the assets it holds because it is effectively distributing ownership rights in those assets to the beneficial interest holders. This transaction is typically effectuated by establishing a separate legal entity that merges the contractual rights in the transferred financial assets and allocates ownership interests in them—the beneficial interests. Therefore, a third-party holder's right to pledge or exchange those beneficial interests is the counterpart of a transferee's right to pledge or exchange the transferred assets themselves. Accordingly, a constraint on the transferee that issues those beneficial interests would not necessarily indicate that the transferor has retained control over the transferred financial assets. As a result, the Board concluded that in cases in which (a) a financial asset is transferred to an entity whose sole purpose is to facilitate a securitization or asset-backed financing and (b) the transferee entity is constrained from pledging or exchanging the asset it receives, the transferor should evaluate whether the third-party beneficial interest holders have the ability to pledge or exchange their beneficial interests.

Amendments Related to Effective Control

A46. One of the conditions for sale accounting is contained in paragraph 9(c) of Statement 140. It specifies that the transferor cannot maintain effective control over the transferred financial assets. Statement 140 and the FASB Special Report, *A Guide to Implementation of Statement 140 on Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities,* provide implementation guidance on whether the transferor has maintained effective control. That guidance addresses specific arrangements and has resulted in numerous requests to clarify whether other arrangements result in the transferor's maintaining effective control. In its deliberations on this Statement, the Board decided that it was not feasible to provide specific guidance on all of the possible arrangements that could be made between the various parties to a transfer of financial assets. As a result, the Board decided to amend paragraph 9(c) to clarify the principle of effective control and how to apply the principle when a transferor has continuing involvement with transferred financial assets. That guidance clarifies that the transferor should evaluate whether the transferor, its consolidated affiliates included in the financial statements being presented, and its agents do not maintain effective control by considering (a) any direct continuing involvement with the transferred financial assets and (b) how to apply the principle in the related implementation guidance in paragraphs 32–54A of Statement 140 and in questions 31–56 of the FASB Special Report. The Board also concluded that the application of paragraph 9(c) should consider the transferor's indirect continuing involvement with the transferred financial assets that could enable it to maintain effective control over the transferred financial assets through an arrangement made with beneficial interest holders of the transferred financial assets.

A47. As discussed earlier, the Board decided to modify the financial-components approach to require that the conditions for sale accounting be applied only to transfers of an entire financial asset, a group of entire financial assets, or a portion of an entire financial asset that meets the definition of a participating interest. The Board considered whether a transferor's effective control over a portion of a financial asset transferred in its entirety should be accounted for partially as a sale and partially as a secured borrowing or as a secured borrowing in its entirety. The Board concluded that to account for a transfer of a financial asset as a sale, the transferor must surrender control over the entire financial asset except in the limited circumstance of a transfer of a portion of a financial asset that meets the definition of a participating interest. The Board reasoned that permitting partial sale/partial secured borrowing treatment would be inconsistent with the revisions to the financial-components approach.

A48. Some respondents to the 2008 Exposure Draft objected to the proposed changes to the financial-components approach and asked the Board to reconsider its decision on the removal of the provisions that permitted partial sale/partial financing accounting in Statement 140. The Board affirmed its decision on partial sale accounting because it conflicts with the requirement that a transferor surrender control over an entire financial asset or a group of entire financial assets except for a portion of an entire financial asset that meets the definition of a participating interest. The Board reasoned that partial sale/partial financing treatment would effectively result in a transferor recognizing a portion of a financial asset that does not meet the definition of a participating interest. Furthermore, the Board also noted that any assets obtained in exchange for a transfer of an entire financial asset accounted for as sale are considered proceeds from the sale. If the transferor maintains effective control over a portion of the asset it has transferred, it would be inappropriate for that portion to be considered proceeds from the sale.

Amendments Related to Initial Measurement of Transferred Financial Assets

Measurement of assets obtained and liabilities incurred

A49. Statement 140 required that beneficial interests held by a transferor be measured by allocating the carrying amount of the transferred financial assets between the financial assets sold and the financial assets retained on the basis of their relative fair values. Paragraph 273 of Statement 140 states that beneficial interests in transferred financial assets are different from the original financial assets but that surrender of control has not occurred for the retained beneficial interests because those interests never left the possession of the transferor. However, Statement 140 requires that certain assets obtained and liabilities incurred be initially measured at fair value even though those assets and liabilities often are related to the transferred financial asset. For example, Statement 140 requires that servicing assets and liabilities be initially recognized at fair value.

A50. After the Board decided to require that Statement 140's conditions for sale accounting be applied only to transfers of an entire financial asset, transfers of groups of entire financial assets, and transfers of a participating interest in an entire financial asset, the Board reconsidered the nature of a transferor's beneficial interest in a transferred financial asset. The Board concluded that any beneficial interest or other asset obtained in a transfer accounted for as a sale should be considered proceeds from the sale because a clear exchange has occurred and, thus, warrants initial measurement of all assets obtained and liabilities incurred at fair value. Accordingly, the Board concluded that if a beneficial interest is obtained in a transfer accounted for as a sale issued by an entity that the transferor does not consolidate, it should be initially measured the same way as other assets obtained and liabilities incurred by a transferor from an entity that the transferor is not required to consolidate.

Measurement of a transferor's participating interest

A51. In considering the measurement of a transferor's participating interest, the Board noted that the transferor's participating interest is not transferred. Rather, only the participating interest sold to third parties is transferred and, therefore, the transferor has surrendered control over only those transferred participating interests. Consequently, the Board decided that the carrying amount of the underlying financial asset should continue to be allocated between the participating interests sold and the transferor's participating interest on the basis of relative fair value.

A52. Some Board members are concerned that some transactions that have similar economic effects could be accounted for differently depending on whether the transaction involves a securitization entity or not. For example, if an entity sells a participating interest directly to a third party, assuming the conditions of paragraphs 8B and 9 of Statement 140, as amended by this Statement, are met, the retained interest would not be remeasured at fair value; rather, the carrying amount would be allocated on the basis of the relative fair value of the portion sold and the portion retained. However, if the transferor sold the whole loan to an unconsolidated entity and took back the same participating interest from the entity, the transferor would measure the beneficial interest at fair value and effectively recognize a gain or loss on the portion retained. Such transactions raise questions about the substance of the arrangement and put pressure on the consolidation guidance for variable interest entities. However, the Board decided not to provide an explicit rule to curb that financial structuring. Rather, the Board decided to add disclosures about assets obtained and liabilities incurred as a result of a transfer accounted for as a sale and noted that the enhanced disclosure requirements would provide adequate information to financial statement users to identify the nature of any of those arrangements.

Removal of Exception for Guaranteed Mortgage Securitizations

A53. FASB Statement No. 65, *Accounting for Certain Mortgage Banking Activities,* as amended by FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* requires that, after the securitization of a mortgage loan held for sale, any retained mortgage-backed securities be classified in accordance with the provisions of Statement 115, even when the transferor holds all of the resulting securities. Statement 140, as amended by Statement 156, requires that a transferor recognize a servicing asset or a servicing liability at fair value if the transferor transfers mortgage loans to a qualifying special-purpose entity in a guaranteed mortgage securitization (regardless of whether the transfer meets the requirements for sale accounting) and holds all the resulting securities and classifies those securities as either available for sale or trading securities.

A54. Constituents told the Board that, in some cases, transferors were applying this exception to similar types of securitizations that involved other types of assets by analogizing to the guidance for guaranteed mortgage securitizations. The Board questioned whether it was appropriate to reclassify a financial asset from a loan to a security when a transferor holds all of the resulting securities. The Board was particularly concerned that the exception enables a transferor to recognize a gain or loss even when the transferor has not met the requirements for sale accounting. As a result, the Board decided to eliminate the exception for guaranteed mortgage securitizations. Transfers that fail to meet any of the conditions for sale accounting must be accounted for as secured borrowings. The Board also notes that the fair value option provided in FASB Statement No. 159, *The*

Fair Value Option for Financial Assets and Financial Liabilities, permits an originator to initially and subsequently measure mortgage loans and other financial assets at fair value.

A55. As a result of the Board's decision to remove this exception, a guaranteed mortgage loan that is securitized should be reclassified as a security only when the securitization meets the requirements for sale accounting in paragraph 9 of Statement 140, as amended by this Statement.

Amendments Related to the Fair Value Practicability Exception

A56. As discussed in the basis for conclusions of FASB Statement No. 157, *Fair Value Measurements,* the Board decided to retain the practicability exceptions for fair value measurements in certain accounting pronouncements within the scope of that Statement, including the exception provided in Statement 140. While the Board acknowledged that practicability exceptions would create inconsistencies, it decided not to address those inconsistencies at that time. The Board concluded that issues about practicability exceptions should be addressed in other agenda projects.

A57. In evaluating whether to retain the practicability exception for measuring fair value in Statement 140, the Board considered the basis for the practicability exception in paragraphs 298 and 299 of that Statement. The Board concluded that the concerns that led to the practicability exception in Statement 140 were addressed with the issuance of Statement 157 and decided to remove the fair value practicability exception in Statement 140 in its entirety.

Disclosures

A58. In developing the enhancements to the disclosure requirements included in this Statement, the Board noted that existing U.S. generally accepted accounting principles (GAAP) already requires numerous disclosures about transfers of financial assets, risks and uncertainties, credit concentrations, derivatives, and assets measured at fair value. However, the Board concluded that some of those disclosures could be enhanced and incorporated directly into Statement 140 to improve compliance, transparency, and enforcement. The Board considered input from various constituent groups but primarily considered the recommendations of financial statement users to develop the enhancements to the disclosures. Additionally, the Board considered existing SEC disclosure requirements, existing or contemplated disclosure requirements of other standard setters (including the IASB), and various other studies and articles on the topic of perceived gaps in the disclosure requirements for transferred financial assets in general. For example, the Board considered certain disclosures included in the April 2008 Senior Supervisors Group Report, *Leading-Practice Disclosures for Selected Exposures,* which was issued by banking commissions and regulators from five countries. The Board noted that the identification of leading practices in the Senior Supervisors Group Report would be useful in developing enhanced disclosures required by this Statement.

A59. Financial statement users told the Board that enhanced disclosures are urgently needed to improve transparency in financial reporting, and they suggested many of the incremental disclosures required by this Statement. Financial statement users also told the Board that they need additional information about a transferor's continuing involvement related to transferred financial assets, regardless of whether the transferor accounts for the transfer of financial assets as a sale or as a secured borrowing.

A60. The Board agreed with those views and developed overall disclosure objectives that a reporting entity must meet because it is not possible to develop specific disclosures that would anticipate all existing and future transactions and forms of continuing involvement that may affect a transferor's financial position, financial performance, and cash flows. The Board also decided that the disclosure objectives should apply to existing disclosures, such as the servicing disclosures that were enhanced by Statement 156.

A61. In addition to providing overall disclosure objectives, the Board decided that it should enhance the specific disclosures already required by Statement 140. The Board believes that specific minimum disclosure requirements are necessary to achieve comparability in financial statements and to meet user requests for certain types of information, especially for securitizations, asset-backed financing arrangements, and similar transfers.

A62. The Board decided to retain the aggregation principle from the 2008 Exposure Draft for the disclosure requirements in this Statement. The Board concluded that the current aggregation guidance (by major asset type) was not adequate because of the different risk characteristics within a major asset type that vary by entity. For example, the Board decided that FSP SOP 94-6-1, *Terms of Loan Products That May Give Rise to a Concentration of Credit Risk,* which was issued after Statement 140, should be considered in determining the level of aggregation of disclosures.

A63. For securitization, asset-backed financing arrangements, and similar transfers accounted for as sales when the transferor has continuing involvement with transferred financial assets, the Board decided to specifically require disclosure of the maximum exposure to loss relating to a transferor's continuing involvement. The Board concluded that this disclosure will provide financial statement users with a better understanding of the risks related to a transferor's continuing involvement. Additionally, the Board noted that this disclosure is consistent with similar disclosures required by Interpretation 46(R), as amended by Statement 167, as well as in other areas of U.S. GAAP for derivatives and guarantees.

A64. The Board also decided to require further disclosure about the characteristics of the assets obtained and liabilities incurred in securitizations, asset-backed financing arrangements, and similar transfers accounted for as sales when the transferor has continuing involvement with the transferred financial assets. The Board concluded that an entity should disclose the nature of the proceeds received in the transfer and the inputs and valuation techniques used to initially measure those proceeds at fair value. The Board decided that those disclosures will provide useful information about how the gain or loss from the sale of transferred financial assets is determined.

A65. Footnote 10 to paragraph 17(f)(4) of Statement 140 provided an exception from the disclosures required by that paragraph if a transferor's only continuing involvement was servicing the transferred financial assets. On the basis of constituent feedback about the difficulty of providing a definition of servicing that would be consistently applied, the Board concluded that footnote 10 should be deleted from Statement 140.

A66. Paragraph 17(f) of Statement 140 requires a description of the transferor's continuing involvement. As a result of the Board's decision to amend paragraph 17(f) of Statement 140 to require a similar disclosure that includes transfers with any continuing involvement in transferred financial assets regardless of when the transfer originally occurred, the Board concluded that the term *continuing involvement* should be explicitly defined in Statement 140. The Board developed the definition of continuing involvement on the basis of examples of what constitutes continuing involvement that were already provided in Statement 140 and in the FASB Special Report on Statement 140.

A67. Respondents to the 2008 Exposure Draft indicated that certain derivatives, such as plain vanilla interest rate swaps and foreign currency derivatives and guarantees, should be excluded from the definition of continuing involvement. Respondents were concerned that this Statement would require additional disclosures for derivatives and guarantees beyond those currently required by other U.S. GAAP because the entity was a transferor. The Board affirmed its tentative decision in the Exposure Draft that derivative instruments entered into contemporaneously with, or in contemplation of, a transfer of financial assets and guarantees represent continuing involvement and decided not to exclude certain derivatives or guarantees from the definition of continuing involvement. However, the Board decided to provide guidance that addresses the interaction between the disclosures required in paragraph 17(f) and the disclosures required by other U.S. GAAP for a specific form of continuing involvement.

A68. In addition to the specific amendments to the disclosure requirements in Statement 140, the Board also considered the effect of the deletion of the qualifying special-purpose entity concept and the related exception from consolidation guidance. The Board noted that this amendment would require additional disclosures if the transferred financial assets involve an entity that is considered to be a variable interest entity under Interpretation 46(R). Accordingly, the Board considered the disclosure enhancements in Interpretation 46(R) and decided that certain disclosures in both Statement 140 and Interpretation 46(R) should be similar.

A69. As noted in paragraph A10 of this Statement, the Board decided to issue separately FSP FAS 140-4 and FIN 46(R)-8, which is superseded by this Statement, in December 2008, to expeditiously meet financial statements user needs for additional information about transfers of financial assets and variable interest entities. After the issuance of the FSP, the Board and FASB staff reviewed a sample of disclosures prepared in accordance with the FSP. They discussed the effectiveness of the FSP with constituents, including preparers, auditors, regulators, and financial statement users, to determine whether the FSP was understandable and whether the enhanced disclosures were providing adequate and useful information to financial statement users. In general, constituents stated that the FSP was understandable and preparers indicated that they were able to obtain the information required by the FSP. Financial statement users stated that the disclosures were a significant improvement, but many of those users indicated that a disclosure about a transferor's continuing involvement was needed for all transfers accounted for as sales within the scope of Statement 140 and not just for securitizations and asset-backed financing arrangements, as required by the FSP. However, other constituents objected to expanding the scope of the specific disclosure requirements to all transfers accounted for as sales in which the transferor had continuing involvement because many of the detailed disclosures would not be relevant since they were developed for securitization and asset-backed financing arrangements. Those constituents stated that the specific disclosures would not be useful and would be overly burdensome for financial statement preparers. As a result, the Board decided to broaden the scope of the disclosure objectives and the application guidance of those objectives, included in paragraphs 16A–16C, to all transfers of financial assets within the scope of Statement 140. For this Statement, the Board also decided to require, at a minimum, specific disclosures about a transferor's continuing involvement with securitizations, asset-backed financing arrangements, and similar transfers.

Effective Date and Transition

A70. The Board concluded that the requirements of this Statement should be effective as soon as reasonably possible for the following reasons:

a. There is an urgent need to improve transparency related to certain entities that are off balance sheet and certain transactions that are currently reported as sales. The Board has received urgent requests from financial statement users; the SEC; the U.S. Senate Banking Subcommittee on Securities, Insurance, and Investments; The President's Working Group on Financial Markets; the Financial Crisis Advisory Group (FCAG); and other constituents that improvements to derecognition and consolidation accounting are required to help restore confidence in the financial markets. In particular, the FCAG, which was convened by the IASB and the FASB, told the Board that immediate improvements are needed to derecognition and consolidation standards followed by a joint effort with the IASB to issue converged standards on derecognition and consolidation. The FCAG told the Board that improvements to the derecognition and consolidation standards will be a significant, lasting, and global advancement in financial reporting.
b. There is significant diversity in practice in applying Statement 140 to transfers of financial assets.
c. Constituents raise frequent application questions about Statement 140.

A71. The Board recognizes that the removal of the qualifying special-purpose entity scope exception from consolidation will require some preparers to gather and analyze significant amounts of data to initially apply the applicable consolidation guidance to those entities. In addition, the Board considered the time needed by other constituents, such as regulators, to analyze the effects of the removal of the qualifying special-purpose entity scope exception and to implement any necessary changes, including potential changes to regulatory capital requirements.

A72. The Board originally considered whether this Statement should be effective for fiscal years beginning after November 15, 2008. However, to have sufficient time to discuss adequately the amendments with preparers, regulators, auditors, and financial statement users, the Board did not issue this Statement until June 2009. The Board noted that preparers, regulators, auditors, and financial statement users need adequate time to consider and implement the amendments and discuss the effect on regulatory requirements, which are based in part on U.S. GAAP. In addition, financial statement users told the Board that they would prefer a single effective date. As a result, the Board decided that this Statement should be effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Additionally, on and after the effective date, existing qualifying special-purpose entities will need to be evaluated for consolidation by reporting entities. Furthermore, the Board decided that the disclosures required by this Statement should be applied to transfers that occurred both before and after the effective date of this Statement. The Board also concluded that it is important to establish the same effective date for both this Statement and Statement 167 because many transactions would be affected by both Statements.

A73. The transaction-based prospective approach used in this Statement for transfers of financial assets is similar to the approach used when Statement 140 was issued and was adopted in this Statement for the same reasons: to achieve consistency in accounting for transfers of financial assets and to ensure that all entities report similar transactions consistently. However, due to the Board's concerns about qualifying special-purpose entities, the Board decided that all existing qualifying special-purpose entities should be evaluated for consolidation on and after the effective date of this Statement. Although the Board realizes that some constituents have requested additional time, the Board decided that for the reasons cited in paragraph A70 of this Statement, the amendments should become effective as soon as reasonably possible.

Benefits and Costs

A74. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement a new standard are borne primarily by present investors. The Board's assessment of the costs and benefits of issuing an accounting standard is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement an accounting standard or to quantify the value of improved information in financial statements. The Board's assessment of this Statement's benefits and costs is based on discussions with preparers, auditors, regulators, and financial statement users. The Board considered the incremental costs of implementing the provisions of this Statement and concluded that those costs do not outweigh the benefits of comparability and simplification.

A75. The most important benefit of this Statement is to provide financial statement users with more relevant, comparable, and transparent information about the present and potential effect of a transferor's continuing involvement in transferred financial assets on the transferor's financial results. Many investors and financial statement users have told the Board there is an urgent need to enhance the information required by Statement 140 to capture the economic substance of the transfers, and some recommended that transferred financial assets remain on the statement of financial position if a transferor has any continuing involvement in the transferred financial assets. They also questioned the credibility of information provided by transferors about transferred financial assets in light of recent market events.

A76. This Statement also will simplify the accounting for transfers of financial assets by removing a complex area of accounting—the concept of a qualifying special-purpose entity—and subjecting all entities to the same accounting literature.

A77. The following are some of the benefits of this Statement:

a. It improves comparability in financial reporting by eliminating the exception for qualifying special-purpose entities from the consolidation guidance. Thus, consistency in the application of consolidation guidance to securitization entities will be improved.
b. It improves consistency in the application of reported financial information by clarifying the requirements for isolation of a transfer of an entire financial asset, a group of entire financial assets, and a participating interest in an entire financial asset.
c. It provides more relevant financial information. For example, it requires initial measurement to be at fair value for beneficial interests received by a transferor if the transfer meets the requirements for sale accounting. This is consistent with the method of measuring other assets and liabilities received as a result of a sale. The requirement that all interests received be initially measured by a single initial measurement attribute also simplifies the accounting for securitizations of financial assets.
d. It requires that a transferor provide additional disclosures to help financial statement users better understand a transferor's continuing involvement with transferred financial assets, the risks inherent in the transferred financial assets that have been transferred or retained, and the nature and financial effect of restrictions on the transferor's assets that continue to be reported in the statement of financial position.

A78. The Board recognizes that some entities may incur significant costs to (a) develop and implement changes to information systems, (b) implement new internal controls, and (c) obtain additional capital to meet regulatory requirements on capital adequacy. In addition, regulators of financial institutions who base certain calculations for capital adequacy on U.S. GAAP financial statements may incur additional time and effort to evaluate the effect of this Statement's changes on those calculations and to make any adjustments that they deem necessary to capital adequacy calculations. The additional disclosures required to report future transfers that are either secured borrowings or sales also may be more costly to prepare and audit. However, the Board believes that the amendments to Statement 140 are necessary to provide relevant, understandable, and transparent financial information to capital markets.

Convergence

A79. Many respondents to the 2008 Exposure Draft stated that the Board should abandon its current project to amend Statement 140 and work with the IASB to develop a converged model on derecognition of financial assets. However, financial statement users told the Board that immediate improvements are vital to provide investors and U.S. capital markets with information about significant exposures related to a transferor's continuing involvement with transferred financial assets. The Board believes that the timetable for a converged standard would not meet the needs of the capital markets for prompt improvement in financial reporting. In addition, the Board believes that the need to eliminate the qualifying special-purpose entity concept overrides the need for a convergent standard. In addition, the Board cited the March 2008 President's Working Group on Financial Markets Policy Statement on Financial Market Developments. That Policy Statement includes a recommendation that states, in part, that "authorities should encourage FASB to evaluate the role of accounting standards in the current market turmoil. This evaluation should include an assessment of the need for further modifications to accounting standards related to consolidation and securitization, with the goal of improving transparency and the operation of U.S. standards in the short-term." As a result, the Board decided to continue its efforts to improve Statement 140 in the short term and at the same time work with the IASB on a long-term, converged standard. This Statement improves convergence by eliminating the concept of a qualifying special-purpose entity, which does not exist in International Financial Reporting Standards, and by narrowing the portions of financial assets that are eligible for derecognition. This project also incorporates certain disclosures currently required by IFRS 7, *Financial Instruments: Disclosures.*

Appendix B

AMENDMENTS TO EXISTING PRONOUNCEMENTS

B1. This appendix includes amendments to authoritative literature affected by the requirements of this Statement. This Statement amends Statement 140 to replace the term *interests that continue to be held by the transferor* with the term *transferor's interests.* Pronouncements affected only by that change in terminology are excluded from this appendix.

B2. This Statement supersedes the following FSPs:

a. FSP FAS 140-2, *Clarification of the Application of Paragraphs 40(b) and 40(c) of FASB Statement No. 140*
b. FSP FAS 140-4 and FIN 46(R)-8, *Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities.*

B3. FASB Statement No. 65, *Accounting for Certain Mortgage Banking Activities,* is amended as follows: [Added text is underlined and deleted text is ~~struck out~~.]

a. Paragraph 6, as amended:

> A mortgage loan transferred to a long-term-investment classification shall be transferred at the lower of cost or fair value on the transfer date. Any difference between the carrying amount of the loan and its outstanding principal balance shall be recognized as an adjustment to yield by the interest method.[2] A mortgage loan shall not be classified as a long-term investment unless the mortgage banking enterprise has both the ability and the intent to hold the loan for the foreseeable future or until maturity. After the securitization of a mortgage loan held for sale~~,~~ that meets the requirements for a sale under paragraph 9 of FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilties,* as amended by FASB Statement No. 166, *Accounting for Transfers of Financial Assets,* any ~~retained~~ mortgage-backed securities received as

proceeds by the transferor shall be classified in accordance with the provisions of FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities.* However, a mortgage banking enterprise must classify as trading any ~~retained~~ mortgage-backed securities received as proceeds that it commits to sell before or during the securitization process. An enterprise is prohibited from reclassifying loans as investment securities unless the transfer of those loans meets the requirements for sale accounting under paragraph 9 of Statement 140, as amended by Statement 166.

B4. FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments,* is amended as follows:

a. Paragraph 3:

~~The primary objective of this Statement with respect to FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* is to eliminate a restriction on the passive derivative instruments that a qualifying special-purpose entity (SPE) may hold.~~

B5. FASB Statement No. 156, *Accounting for Servicing of Financial Assets,* is amended as follows:

a. Paragraph 2:

An entity shall apply this Statement to all separately recognized servicing assets and servicing liabilities. This Statement requires that an entity separately recognize a servicing asset or servicing liability when it undertakes an obligation to service a financial asset by entering into a servicing contract in connection with ~~any~~either of the following situations:

a. A servicer's transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire ~~the servicer's~~ financial asset~~s~~ that meets the requirements for sale accounting; or
~~b. A transfer of the servicer's financial assets to a qualifying special-purpose entity in a guaranteed mortgage securitization in which the transferor retains all of the resulting securities and classifies them as either available-for-sale securities or trading securities in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*~~
c. An acquisition or assumption of an obligation to service a financial asset that does not relate to financial assets of the servicer or its consolidated affiliates included in the financial statements being presented.

An entity that transfers its financial assets ~~to a qualifying special-purpose entity in a guaranteed mortgage securitization~~ to an unconsolidated entity in a transfer that qualifies as a sale in which the transferor ~~retains all of~~ obtains the resulting securities and classifies them as debt securities held-to-maturity in accordance with Statement 115 may either separately recognize its servicing assets or servicing liabilities or report those servicing assets or servicing liabilities together with the asset being serviced.

b. Paragraph 3(b):

Contractually specified servicing fees
All amounts that, per contract, are due to the servicer in exchange for servicing the financial asset and would no longer be received by a servicer if the beneficial owners of the serviced assets (or their trustees or agents) were to exercise their actual or potential authority under the contract to shift the servicing to another servicer. Depending on the servicing contract, those fees may include some or all of the difference between the interest rate collectible on the financial assets being serviced and the rate to be paid to the beneficial owners of those financial assets.

c. Paragraph 3(d):

Financial asset
Cash, evidence of an ownership interest in an entity, or a contract that conveys to one ~~a second~~ entity a ~~contractual~~ right (1) to receive cash or another financial instrument from a second ~~first~~ entity or (2) to exchange other financial instruments on potentially favorable terms with the second ~~first~~ entity ~~(Statement 107, paragraph 3(b))~~.

d. Paragraph 3(e):

~~**Guaranteed mortgage securitization**~~
~~A securitization of mortgage loans that is within the scope of FASB Statement No. 65,~~

~~*Accounting for Certain Mortgage Banking Activities,* as amended, and includes a substantive guarantee by a third party.~~

e. Paragraph 3(g):

Proceeds
Cash, beneficial interests, servicing assets, derivatives, or other assets that are obtained in a transfer of financial assets, less any liabilities incurred.

f. Paragraph 3(m):

~~**Undivided interest**~~
~~Partial legal or beneficial ownership of an asset as a tenant in common with others. The proportion owned may be pro rata, for example, the right to receive 50 percent of all cash flows from a security, or non–pro rata, for example, the right to receive the interest from a security while another has the right to the principal.~~

B6. FASB Statement No. 157, *Fair Value Measurements,* is amended as follows:

a. Footnote 2, as amended, to paragraph 2:

Accounting pronouncements that permit practicability exceptions to fair value measurements in specified circumstances include APB Opinion No. 29, *Accounting for Nonmonetary Transactions,* FASB Statements No. 87, *Employers' Accounting for Pensions,* No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions,* No. 107, *Disclosures about Fair Value of Financial Instruments,* No. 116, *Accounting for Contributions Received and Contributions Made,* ~~No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,*~~ No. 141 (revised 2007), *Business Combinations,* No. 143, *Accounting for Asset Retirement Obligations,* No. 146, *Accounting for Costs Associated with Exit or Disposal Activities,* and No. 153, *Exchanges of Nonmonetary Assets,* and FASB Interpretations No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others,* and No. 47, *Accounting for Conditional Asset Retirement Obligations*. Also included among those pronouncements are AICPA Audit and Accounting Guide, *Not-for-Profit Organizations,* and EITF Issues No. 85-40, "Comprehensive Review of Sales of Marketable Securities with Put Arrangements," and No. 99-17, "Accounting for Advertising Barter Transactions."

B7. FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities,* is amended as follows:

a. Paragraph 4(c):

~~Neither a transferor of financial assets nor its affiliates shall consolidate a qualifying special-purpose entity as described in paragraph 35 of FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* or a "formerly qualifying SPE" as described in paragraph 25 of Statement 140. A transferor reports its rights and obligations related to the qualifying special-purpose entity according to the requirements of Statement 140.~~

b. Paragraph 4(d):

~~An enterprise that holds variable interests in a qualifying special-purpose entity or a "formerly qualifying SPE," as described in paragraph 25 of Statement 140, shall not consolidate that entity unless that enterprise has the unilateral ability to cause the entity to liquidate or to change the entity so that it no longer meets the conditions in paragraph 25 or 35 of Statement 140. If the entity is not consolidated, the enterprise reports its rights and obligations related to the entity.~~

c. Footnote 27 to paragraph B26:

~~This analysis describes variable interests in all variable interest entities including qualifying special-purpose entities. However, a special requirement applies to qualifying special-purpose entities. Refer to paragraphs 4(c) and 4(d).~~

B8. FASB Technical Bulletin No. 87-3, *Accounting for Mortgage Servicing Fees and Rights,* is amended as follows:

a. Paragraph 9, as amended:

> An enterprise should separately recognize either a servicing asset or a servicing liability each time that it undertakes an obligation to service a financial asset by entering into a servicing contract in ~~any~~either of the following situations:
>
> a. A servicer's transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire ~~the servicer's~~ financial asset~~s~~ that meets the requirements for sale accounting; or
>
> ~~b. A transfer of the servicer's financial assets to a qualifying special-purpose entity (SPE) in a guaranteed mortgage securitization in which the transferor retains all of the resulting securities and classifies them as either available-for-sale securities or trading securities in accordance with FASB Statement No. 115,~~ ~~*Accounting for Certain Investments in Debt and Equity Securities*~~
>
> c. An acquisition or assumption of an obligation to service a financial asset ~~a servicing obligation~~ that does not relate to financial assets of the servicer or its consolidated affiliates included in the financial statements being presented.
>
> Servicing assets that are subsequently measured using the amortization method are amortized in proportion to, and over the period of, estimated net servicing income—the excess of servicing revenues over servicing costs. Servicing liabilities that are subsequently measured using the amortization method are amortized in proportion to, and over the period of, estimated net servicing loss—the excess of servicing costs over servicing revenues. For servicing assets and servicing liabilities that are subsequently measured using the fair value measurement method, changes in fair value of servicing assets and servicing liabilities shall be reported in earnings in the period in which the changes occur. An entity that transfers its financial assets ~~to a qualifying SPE in a guaranteed mortgage securitization~~ to an unconsolidated entity in a transfer that qualifies as a sale in which the transferor retains all of the resulting debt securities and classifies them as held-to-maturity in accordance with Statement 115 either may separately recognize its servicing assets or servicing liabilities or may report those servicing assets or servicing liabilities together with the asset being serviced.

B9. Statement 133 Implementation Issue No. D1, *Application of Statement 133 to Beneficial Interests in Securitized Financial Assets,* is amended as follows:

a. The fifth paragraph of the Response section:

> Given the issues outlined above, the staff believes the interpretation of the scope exception in paragraph 14 of Statement 133 and the determination of whether beneficial interests in securitized financial assets meet the definition of a derivative are complex issues that warrant further study. ~~Further, if it is determined that some of those beneficial interests do not meet the definition of a derivative in its entirety, the staff believes further study may be required to determine whether the guidance in Statement 133 Implementation Issue No. B12, "Beneficial Interests Issued by Qualifying Special-Purpose Entities," is adequate to determine whether the beneficial interest has an embedded derivative that must be accounted for separately under paragraph 12 of Statement 133.~~

b. The seventh paragraph of the Response section:

> Pending further guidance on those questions, entities may continue to apply the guidance related to accounting for beneficial interests in paragraph 14 and paragraph 362 of Statement 140. Paragraph 14 (as amended) states, "Financial assets, except for instruments that are within the scope of Statement 133, that can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment shall be subsequently measured like investments in debt securities classified as available-for-sale or trading under Statement 115. Examples of such financial assets include, but are not limited to, interest-only strips, other beneficial interests ~~Interest-only strips, other interests that continue to be held by a transferor in securitizations~~, loans, or other receivables~~, or other financial assets that can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment, except for instruments that are within~~

~~the scope of Statement 133, shall be subsequently measured like investments in debt securities classified as available-for-sale or trading under Statement 115. . . .~~"[2] Paragraph 362 of Statement 140 amends Statement 115 similarly to indicate that any security that can be contractually prepaid or otherwise settled in such a way that the holder of the security would not recover substantially all of its recorded investment may not be classified as held-to-maturity. ~~The interim guidance is not limited to securitizations involving qualifying special-purpose entities.~~

c. The first paragraph of the Effective Date and Transition section:

Statement 155, which was issued in February 2006, addresses issues on the evaluation of beneficial interests issued in securitization transactions under Statement 133. Specifically, Statement 155 amends Statement 133 to establish a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation. The FASB staff interim guidance in this Implementation Issue remains effective only for instruments recognized prior to the effective date of Statement 155. This Implementation Issue has not been updated for amendments to Statement 133 after the issuance of Statement 155. In addition, the Implementation Issue has not been updated for amendments to Statement 140, as amended by FASB Statement No. 166, *Accounting for Transfers of Financial Assets,* except for the fifth and seventh paragraphs of the Response section.

B10. Statement 133 Implementation Issue No. F8, *Hedging Mortgage Servicing Right Assets Using Preset Hedge Coverage Ratios,* is amended as follows:

a. The second paragraph of the Background section:

Servicing rights are contracts to service loans, receivables, or other financial assets under which the servicer is obligated to perform specific administration functions and is compensated with contractually specified servicing fees. Servicing rights are separately recognized as either servicing assets or servicing liabilities when an entity undertakes an obligation to service a financial asset by entering into a servicing contract in ~~any~~either of the following situations as stated in paragraph 13 of FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* (as amended by Statement 156):

a. A servicer's transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire ~~the servicer's~~ financial asset~~s~~ that meets the requirements for sale accounting; or

~~b. A transfer of the servicer's financial assets to a qualifying SPE [special-purpose entity] in a **guaranteed mortgage securitization** in which the transferor retains all of the resulting securities and classifies them as either available-for-sale securities or trading securities in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*~~

c. An acquisition or assumption of a servicing obligation that does not relate to financial assets of the servicer or its consolidated affiliates included in the financial statements being presented.

An entity that transfers its financial assets ~~to a qualifying special-purpose entity in a guaranteed mortgage securitization~~ to an unconsolidated entity in a transfer that qualifies as a sale in which the transferor ~~retains all of~~ obtains the resulting securities and classifies them as debt securities held-to-maturity in accordance with Statement 115 may either separately recognize its servicing assets or servicing liabilities or report those servicing assets or servicing liabilities together with the asset being serviced.

Appendix C

AMENDMENTS TO OTHER AUTHORITATIVE LITERATURE

C1. This appendix addresses the effect of this Statement on authoritative accounting literature included in categories (*b*), (*c*), and (*d*) in the GAAP hierarchy as discussed in FASB Statement No. 162, *The Hierarchy of Generally Accepted Accounting Principles.* This appendix includes the FASB Special Report, *A Guide to Implementation of Statement 140 on Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* marked to integrate changes from this Statement. This appendix also includes the amendments to Emerging Issues Task Force (EITF) Issues and Topics that are affected by the issuance of this Statement. Any authoritative literature affected by the issuance of this Statement solely due to changes in terminology (for example, the replacement of the term *interests that continue to be held by a transferor* with the term *transferor's interest*) has been excluded from this appendix.

C2. The Special Report on Statement 140 is amended as follows: [Added text is underlined and deleted text is ~~struck out~~.]

INTRODUCTION

In September 2000, the Financial Accounting Standards Board (FASB) issued Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* which replaces Statement 125 but carries over most of its provisions without reconsideration.

Questions of implementation on a new standard are often raised with the FASB staff by preparers, auditors, and others. The staff determined that this Special Report should be issued as an aid in understanding and implementing Statement 140 because of the relatively high number of inquiries received on that Statement and Statement 125.

The questions and answers in this Special Report are organized by the general topics in Statement 140 to which they relate. This Special Report is a cumulative document: it incorporates both new questions and answers and updated questions and answers from the first, second, and third editions of the Special Report, *A Guide to Implementation of Statement 125 on Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* and questions and answers from EITF Topic No. D-94, "Questions and Answers Related to the Implementation of FASB Statement No. 140.~~;~~" ~~and EITF Topic No. D-99, "Questions and Answers Related to Servicing Activities in a Qualifying Special-Report under FASB Statement No. 140."~~

In March 2006, the FASB issued FASB Statement No. 156, *Accounting for Servicing of Financial Assets.* Statement 156 requires all separately recognized servicing assets and servicing liabilities to be initially measured at fair value~~, if practicable,~~ and permits an entity to subsequently measure those servicing assets and servicing liabilities at fair value. The questions and answers in this Special Report have been updated to reflect changes resulting from the issuance of Statement 156.

In June 2009, the FASB issued Statement No. 166, *Accounting for Transfers of Financial Assets.* Statement 166 amends Statement 140 to, among other things, modify the financial-components approach, remove the concept of a qualifying special-purpose entity, clarify the isolation and effective control conditions for sale accounting in paragraph 9 of Statement 140, amend initial measurement of a transferor's interest in transferred financial assets, and require additional disclosures. The questions and answers in this Special Report have been updated to reflect changes resulting from the issuance of Statement 166.

QUESTIONS AND ANSWERS

Scope

1. *Q*—If a right to receive the minimum lease payments to be received under an operating lease is transferred, could it be considered a financial asset within the scope of Statement 140?

   A—No. A right to receive the minimum lease payments to be received under an operating lease is an unrecognized financial asset. As stated in paragraph 4, Statement 140 "does not address . . . transfers of unrecognized financial assets, for example, minimum lease payments to be received under operating leases."

2. *Q*—Is a transfer of servicing rights that are contractually separated from the underlying serviced assets within the scope of Statement 140? For example, does Statement 140 apply to an entity's conveyance of mortgage servicing rights that have been separated from an underlying mortgage loan portfolio that the entity intends to retain?

   A—No. Paragraph 4 states that Statement 140 "does not address transfers of nonfinancial assets, for example, servicing assets. . . ." <u>(See AICPA Statement of Position 01-6, *Accounting by Certain Entities (Including Entities with Trade Receivables) That Lend to or Finance the Activities of Others,* and EITF Issue</u> ~~The Board's conclusion is reiterated in the Status sections of EITF Issues No. 85-13, "Sale of Mortgage Service Rights on Mortgages Owned by Others," No. 87-34, "Sale of Mortgage Servicing Rights with a Subservicing Agreement," No. 90-21, "Balance Sheet Treatment of a Sale of Mortgage Servicing Rights with a Subservicing Agreement," and~~ No. 95-5, "Determination of What Risks and Rewards, If Any, Can Be Retained and Whether Any Unresolved Contingencies May Exist in a Sale of Mortgage Loan Servicing Rights."<u>) [Revised 6/09.]</u>

3. *Q*—Is a debtor's conveyance of cash or noncash financial assets in full or partial settlement of an obligation to a creditor a *transfer* under Statement 140?

   A—No. A payment of cash or a conveyance of noncash financial assets to the holder of a loan or other receivable in full or partial settlement of an obligation is not a transfer under Statement 140.[1]

   To explain, a transfer, as defined in paragraph 364, is "the conveyance of a noncash financial asset by and to someone other than the issuer of that financial asset." Conveyances that do not meet the definition of a transfer include the origination of a receivable, the settlement of that receivable, or the restructuring of that receivable into a security in a troubled debt restructuring. A cash payment or conveyance of noncash financial assets from a debtor to a creditor results in full or partial settlement of the creditor's receivable from the debtor. Therefore, <u>that conveyance</u> ~~the conveyance of assets~~ is not a transfer ~~and, thus, not~~ within the scope of Statement 140's provisions for transfers of financial assets. However, if a noncash financial asset was conveyed to the creditor in full or partial settlement of a creditor's receivable, it would be rare to conclude that debt has been extinguished if the ~~criteria~~ <u>conditions</u> of paragraph 9 were not also met. <u>[Revised 6/09.]</u>

4. *Q*—Does Statement 140 address a reacquisition by an entity of its own securities by exchanging noncash financial assets (for example, U.S. Treasury bonds or shares of an unconsolidated investee) for its common shares?

   A—No. Paragraph 4 states that "this Statement does not address . . . investments by owners or distributions to owners of a business enterprise." That scope exclusion applies to both the transferor and the transferee. The transaction in question constitutes a distribution by an entity to its owners, as defined in FASB Concepts Statement No. 6, *Elements of Financial Statements,* and, therefore, is excluded from the scope of Statement 140.

5. *Q*—Do the provisions of Statement 140 apply to "desecuritizations" of securities into loans or other financial assets?

   A—Statement 140 does not specifically address the accounting for desecuritization transactions. EITF Topic No. D-51, "The Applicability of FASB Statement No. 115 to Desecuritizations of Financial Assets," addresses that issue.

6. *Q*—The deregulation of utility rates charged for electric power generation has caused electricity-producing companies to identify some of their electric power generation operations as "stranded costs." Prior to deregulation, utilities typically expected to be reimbursed for costs through regulation of rates charged to customers. After deregulation, some of these costs may no longer be recoverable through unregulated rates. Hence, such potentially unrecoverable costs often are referred to as stranded costs. However, some of those stranded costs may be recovered through a surcharge or tariff imposed on rate-regulated goods or services provided by another portion of the entity whose pricing remains regulated.

[1]Whether or not that settlement is an extinguishment is governed by paragraph 16 of Statement 140.

Some entities have securitized their enforceable rights to impose that tariff (often referred to as "securitized stranded costs"), thereby obtaining cash from investors in exchange for the future cash flows to be realized from collecting surcharges imposed on customers of the rate-regulated goods or services. Are securitized stranded costs considered to be financial assets, the transfer of which would be within the scope of Statement 140?

A—No. Paragraph 364 defines *financial asset* as ". . . a *contract* that conveys to ~~a second~~ one entity a ~~*contractual*~~ *right* (a) to receive cash or another financial instrument from ~~first~~ a second entity or (b) to exchange other financial instruments on potentially favorable terms with the ~~first~~ second entity" (emphasis added). Therefore, to be a financial asset, an asset must arise from a contractual agreement between two or more parties, not by an imposition of an obligation by one party on another. This notion in Statement 140 is consistent with the notion discussed in paragraph 39 of FASB Statement No. 105, *Disclosure of Information about Financial Instruments with Off-Balance-Sheet Risk and Financial Instruments with Concentrations of Credit Risk,*[2] which stated:

> Other contingent items that ultimately may require the payment of cash but do not as yet arise from contracts, such as contingent liabilities for tort judgments payable, are not financial instruments. However, when those obligations become enforceable by government or courts of law and are thereby contractually reduced to fixed payment schedules, the items would be financial instruments under the definition.

[Revised 6/09.]

Securitized stranded costs are not financial assets, and therefore transfers of securitized stranded costs are not within the scope of Statement 140. Securitized stranded costs are not financial assets because they are imposed on ratepayers by a state government or its regulatory commission and, thus, while an enforceable right for the utility, they are not a *contractual* right to receive payments from another party. To elaborate, while a right to collect cash flows exists, *it is not the result of a contract* and, thus, not a financial asset. Refer to Question 7.

7. *Q*—Would a transfer of *beneficial interests* in a securitization trust that holds nonfinancial assets such as securitized stranded costs or other similar rights by third-party investors be within the scope of Statement 140?

   A—Yes. The beneficial interests in a securitization trust that holds nonfinancial assets such as securitized stranded costs or other similar imposed rights would be considered financial assets by the third-party investors, unless that third party must consolidate[3] the trust.

8. *Q*—Is a judgment from litigation a financial asset?

   A—Generally, no, but the answer depends on the facts and circumstances. Consistent with the notion in paragraph 39 of Statement 105,[4] a contingent receivable that ultimately may require the payment of cash but does not as yet arise from a contract (such as a contingent receivable for a tort judgment) is not a financial asset. However, when that judgment becomes enforceable by a government or a court of law and is thereby *contractually* reduced to a fixed payment schedule, the judgment would be a financial asset. To elaborate, if and when the parties agree to payment terms and those payment terms are reduced to a contract, then a financial asset exists.

9. *Q*—Is a judgment from litigation a financial asset if it is transferred to an unrelated third party (that is, would the transfer be within the scope of Statement 140)?

   A—Yes, but only if that judgment is enforceable by a government or a court of law and has been contractually reduced to a fixed payment schedule. Refer to Question 8.

[2]Although Statement 105 was superseded by FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities,* the Board's definition of *financial asset* continues to be based on the definition of a financial instrument found in Statement 105.

[3]FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities,* as amended by FASB Statement No. 167, *Amendments to FASB Interpretation No. 46(R),* should be applied, together with other guidance on consolidation policy, as appropriate, to determine whether such an ~~special-purpose~~ entity should be consolidated by a third-party investor. [Revised 4/03; 6/09.]

[4]Refer to footnote 2.

10. *Q*—Does Statement 140 apply to a transfer of an ownership interest in a consolidated subsidiary by its parent if that consolidated subsidiary holds nonfinancial assets?

    A—No. An ownership interest in a consolidated subsidiary is evidence of control of the entity's individual assets and liabilities, not all of which are financial assets, and Statement 140 only applies to transfers of financial assets and extinguishments of liabilities. (Note that in the parent's [transferor's] consolidated financial statements, the subsidiary's holdings are reported as individual assets and liabilities instead of as a single investment.)

11. [Deleted 8/01 because FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets,* eliminates the concept of temporary control.]

12. *Q*—Would Statement 140 apply to a transfer of an investment in a controlled entity that has not been consolidated by an entity because that entity accounts for its investment in the controlled entity at fair value (for example, a broker-dealer or an investment company)?

    A—Generally, yes.[5a] An entity that carries an investment in a subsidiary at fair value will realize its investment by disposing of it rather than by realizing the values of the underlying assets through operations. Therefore, a transfer of an investment in a subsidiary by that entity is a transfer of the investment (a financial asset), not the underlying assets and liabilities (which might include nonfinancial assets).~~ Refer to Question 11.~~ [Revised 9/01; 6/09.]

13. *Q*—Is a transfer of an equity method investment within the scope of Statement 140?

    A—Yes, unless the transfer is of an investment that is in substance a sale of real estate, as defined in FASB Interpretation No. 43, *Real Estate Sales.*

    For transfers of investments that are in substance a sale of real estate, refer to FASB Statement No. 66, *Accounting for Sales of Real Estate,* APB Opinion No. 29, *Accounting for Nonmonetary Transactions,* and EITF Issue No. 01-2, "Interpretations of APB Opinion No. 29." [Revised 9/01; 5/03; 4/05.]

14. *Q*—Is a forward contract on a financial instrument that must be (or may be) physically settled by the delivery of that financial instrument in exchange for cash a financial asset or financial liability, the transfer (or extinguishment in the case of a liability) of which would be within the scope of Statement 140?

    A—Yes. Under Statement 140, a *financial asset* is "cash, evidence of an ownership interest in an entity, or a contract that conveys to ~~a second~~ one entity a ~~contractual~~ right (a) to receive cash or another financial instrument from a ~~first~~second entity or (b) to exchange other financial instruments on potentially favorable terms with the ~~first~~second entity" (paragraph 364). Statement 140 defines *financial liability* as "a contract that imposes on one entity ~~a contractual~~an obligation (a) to deliver cash or another financial instrument to a second entity or (b) to exchange other financial instruments on potentially unfavorable terms with the second entity" (paragraph 364). [Revised 6/09.]

    Under those definitions, a forward contract to purchase or sell a financial instrument that must be (or may be) net settled or physically settled by exchanging that financial instrument for cash (or some other financial asset) is a financial asset or financial liability.

15. *Q*—Is a transfer of a recognized financial instrument that may be a financial asset or a financial liability at any given point in time, such as a forward or swap contract, subject to the provisions of both paragraph 9 and paragraph 16?

    A—Yes. Statement 140 provides guidance on transfers of financial assets and extinguishments of liabilities in paragraph 9 and paragraph 16, respectively. Certain recognized financial instruments, such as forward and swap contracts, have the potential to be financial assets or financial liabilities. Accordingly,

[5a]~~See footnote 4a.~~One exception is a transfer of an investment that is in-substance real estate, as defined in FASB Interpretation No. 43, *Real Estate Sales.* [Revised 6/09.]

transfers of those financial instruments must meet the ~~criteria~~ conditions of both paragraph 9 and paragraph 16 to be derecognized. [Revised 6/09.]

16. *Q*—Does Statement 140 apply to a transfer of a recognized derivative instrument that is not a financial instrument?

A—Yes. Derivative instruments that are nonfinancial liabilities (for example, a written commodity option) are included in the scope of Statement 140 because paragraph 16 applies to extinguishments of *all* liabilities.

Although transfers of nonfinancial assets are not within the scope of Statement 140, the EITF reached a consensus in Issue No. 99-8, "Accounting for Transfers of Assets That Are Derivative Instruments but That Are Not Financial Assets," that transfers of all assets that are nonfinancial derivative instruments subject to the requirements of FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities,* should be accounted for by analogy to Statement 125. Statement 125 was replaced by Statement 140 without reconsideration of this matter. Statement 166 amended Statement 140 without reconsideration of this matter. Therefore, paragraph 9 and the other provisions of Statement 140 should be applied to determine whether a transferred nonfinancial derivative asset (for example, a purchased commodity option) that is accounted for under Statement 133 should be derecognized. [Revised 6/09.]

Similarly, the logic in Question 15 should be applied to transfers of nonfinancial derivative instruments that have the potential to become either assets or liabilities (for example, forward and swap contracts).

Control ~~Criteria~~Conditions

Isolation

17. *Q*—What type of evidence is sufficient to provide reasonable assurance that transferred financial assets are isolated beyond the reach of the transferor and its consolidated affiliates under Statement 140? [Revised 6/09.]

A—~~Statement 140 does not provide guidance as to the type and amount of evidence that must be obtained to conclude that transferred financial assets have been isolated from the transferor according to the criterion of paragraph 9(a).~~ Paragraph 27 states that "derecognition of transferred financial assets is appropriate only if the available evidence provides *reasonable assurance* that the transferred financial assets *would be* beyond the reach of the powers of a bankruptcy trustee or other receiver for the transferor or any of its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented and its creditors . . ." (emphasis added). ~~Further, p~~Paragraph 27 explains that the nature and extent of support to satisfy this assertion depends on the facts and circumstances of each transaction and that all available evidence that either supports or questions an assertion ~~should~~ shall be considered. Further, paragraph 27A describes, in the context of U.S. bankruptcy laws, legal opinions that may be required to conclude that the transferred financial assets have been isolated. Additionally, paragraph 27B states that "for entities that are subject to other possible bankruptcy, conservatorship, or other receivership procedures (for example, banks subject to receivership by the Federal Deposit Insurance Corporation [FDIC]) in the United States or other jurisdictions, judgments about whether transferred financial assets have been isolated need to be made in relation to the powers of bankruptcy courts or trustees, conservators, or receivers in those jurisdictions." [Revised 6/09.]

In December 1997, the Audit Issues Task Force Working Group of the AICPA issued an Auditing Interpretation, "The Use of Legal Interpretations As Evidential Matter to Support Management's Assertion That a Transfer of Financial Assets Has Met the Isolation Criterion in Paragraph 9(a) of Statement of Financial Accounting Standards No. 125," to assist auditors in evaluating whether the available evidence provides reasonable assurance that the transferred financial assets would be beyond the reach of the powers of a bankruptcy trustee or other receiver. That Auditing Interpretation has not been updated to reflect the issuance of Statement 166. For entities that would be subject to FDIC receivership, refer to Question 19. [Revised 6/09.]

18. *Q*—Is the requirement of paragraph 9(a) satisfied if the likelihood of bankruptcy is remote?

A—No. The requirement of paragraph 9(a) would not be satisfied simply because the likelihood of bankruptcy of the transferor is determined to be remote. The requirement of paragraph 9(a) focuses on whether transferred financial assets would be isolated from the transferor in *the event of bankruptcy or other receivership* regardless of how remote or probable bankruptcy or other receivership is at the date of transfer. Paragraph 27 explains that "derecognition of transferred financial assets is appropriate only if the available evidence provides reasonable assurance that the transferred financial assets would be beyond the reach of the powers of a bankruptcy trustee or other receiver for the transferor or any of its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented and its creditors.~~ of the transferor. . . .~~" [Revised 6/09.]

19. *Q*—Can transferred financial assets be isolated from the transferor if the Federal Deposit Insurance Corporation (FDIC) would be the receiver should the transferor fail?

A—Yes, depending on the facts and circumstances. Before July 2000, this situation was unclear. In July 2000, the FDIC adopted a final rule, *Treatment by the Federal Deposit Insurance Corporation as Conservator or Receiver of Financial Assets Transferred by an Insured Depository Institution in Connection with a Securitization or Participation.* That final rule modifies the FDIC's receivership powers so that, subject to certain conditions, it shall not recover, reclaim, or recharacterize as property of the institution or the receivership any financial assets transferred by an insured depository institution that meet all conditions for sale accounting treatment under GAAP, other than the "legal isolation" condition in connection with a securitization or participation.

Paragraphs 159 and 160 of Statement 140 explain that, in light of the FDIC's issuance of this rule, further specific guidance on this issue is not required. ~~Therefore, the Board removed the guidance that was contained in paragraphs 58 and 121 of Statement 125.~~ [Revised 6/09.]

Therefore, the guidance in paragraphs 27–~~,~~ 28~~,~~ and 80–84 of Statement 140 applies to transfers by all entities, including institutions for which the FDIC would be the receiver. ~~Subsequent to the issuance of Statement 140, several questions arose regarding the meaning of paragraphs 27, 28 and 80-84. In response the FASB staff issued additional implementation guidance (see Questions 19A-19D). See also FASB Technical Bulletin 01-1, *Effective Date for Certain Financial Institutions of Certain Provisions of Statement 140 Related to the Isolation of Transferred Financial Assets.*~~ [Revised 9/01; 6/09.]

The Audit Issues Task Force Working Group of the AICPA has issued an Auditing Interpretation, "The Use of Legal Interpretations As Evidential Matter to Support Management's Assertion That a Transfer of Financial Assets Has Met the Isolation Criterion in Paragraph 9(a) of Statement of Financial Accounting Standards No. 140." That ~~update~~ Auditing Interpretation will assist auditors in determining whether the available evidence provides reasonable assurance that the transferred financial assets would be beyond the reach of the powers of the FDIC in light of the FDIC rule. That Auditing Interpretation has not been updated to reflect the issuance of Statement 166. [Revised 9/01; 6/09.]

19A.~~*~~ *Q*—Can financial assets transferred by an entity subject to possible receivership by the FDIC be considered isolated from the transferor (that is, can the transfer meet the condition in paragraph 9(a)) if circumstances can arise under which *the FDIC or another creditor* can require their return? [Revised 6/09.]

A—Yes. Financial ~~A~~assets transferred by an entity subject to possible receivership by the FDIC are isolated from the transferor if the FDIC or another creditor either cannot require return of the transferred financial assets or can

~~*Questions and answers 19A–19D are identical to Questions 1–4 respectively in Appendix B of Technical Bulletin 01-1. They are subject to the effective date provisions of that Technical Bulletin.~~

only require return in receivership, after a default, and in exchange for payment of, at a minimum, principal and interest earned (at the contractual yield) to the date investors are paid. However, see Question 19C for guidance if the transferor can require the return of the transferred financial assets. [Added 9/01~~.]~~; revised 6/09.]

19B.* *Q*—Does the answer to Question 19A also apply to financial assets transferred by an entity subject to *the U.S. Bankruptcy Code?* [Revised 6/09.]

A—No. Paragraphs 81–83 make clear what is needed for transfers by entities subject to the U.S. Bankruptcy Code to meet the condition in paragraph 9(a) that the transferred financial assets have been "put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy. . . ." That result differs from the result for an entity subject to possible receivership by the FDIC discussed in Question 19A. However, given the unusual nature of receivership under the FDIC, the Board did not object to that distinction. [Added 9/01~~.]~~; revised 6/09.]

19C.* *Q*—Can financial assets transferred by any entity be considered isolated from *the transferor* (that is, can the transfer meet the condition in paragraph (9a)) if circumstances can arise under which *the transferor* can require their return, but only in exchange for payment of principal and interest earned (at the contractual yield) to the date investors are paid? [Revised 6/09.]

A—No, unless the transferor's power to require the return of the transferred financial assets arises solely from a contract with the transferee.[6a] The answer is no, even if the noncontractual power appears unlikely to be exercised or is dependent upon the uncertain future actions of other entities (for example, insufficiency of collections on underlying transferred financial assets or determinations by court of law). Such a noncontractual power is inconsistent with the limitations of paragraph 9(a) of Statement 140 that, to be accounted for as having been sold, transferred financial assets must be isolated from the transferor. [Revised 6/09.]

The FASB staff is aware that, under the answer, "single-step" securitizations commonly used by financial institutions subject to receivership by the FDIC and sometimes used by other entities are likely not to be judged as having isolated the assets. One reason for that is because it would be difficult to obtain reasonable assurance that the transferor would be unable to recover the transferred financial assets under the "equitable right of redemption" available to secured debtors, after default, under U.S. Law. [Added 9/01~~.]~~; revised 6/09.]

19D.* *Q*—Which of the ~~those~~ answers in questions 19A–19C applies to entities subject to possible receivership under jurisdictions other than the FDIC or the U.S. Bankruptcy Code? [Revised 6/09.]

A—The answer depends on the circumstances that apply to those types of entities. Paragraph 84 of Statement 140 states, "For entities that are subject to other possible bankruptcy, conservatorship, or other receivership procedures in the United States or other jurisdictions, judgments about whether transferred financial assets have been isolated need to be made in relation to the powers of bankruptcy courts or trustees, conservators, or receivers in those jurisdictions." The same sorts of judgments may need to be made in relation to powers of the transferor or its creditors. [Added 9/01~~.]~~; revised 6/09.]

20. *Q*—~~Would~~ Could a transfer from one subsidiary (the transferor) to another subsidiary (the transferee) of a common parent be accounted for as a sale in ~~the transferor~~ each subsidiary's separate-company financial statements? [Revised 6/09.]

A—Yes, if (a) all of the conditions in paragraph 9 (including the condition on isolation of the transferred financial assets) are met and

[6a] A transferor's power to require the return of the transferred financial assets arising solely from a contract with the transferee, for example, a call option or removal-of-accounts provision, would not necessarily preclude a conclusion that transferred financial assets have been isolated from the transferor. However, under paragraph 9(c) of Statement 140, such a power might preclude sale treatment if through it the transferor maintains effective control over the transferred financial assets. [Revised 6/09.]

(b) the transferee's assets and liabilities are not consolidated into the separate-company financial statements of the transferor. ~~Paragraph 27 explains that derecognition of transferred financial assets is only appropriate when the assets are isolated from the "transferor or *any consolidated affiliate of the transferor*[7] that is not a special-purpose corporation or other entity designed to make remote the possibility that it would enter bankruptcy or other receivership" (emphasis added).~~[8]In applying paragraph 9, the transferor-subsidiary shall not consider parent involvements with the transferred financial assets (see paragraph 26A). [Revised 6/09.]

If the transferee was an equity method investee of the transferor, only the investment and not the investee's assets and liabilities would be reported in the transferor subsidiary's separate-company financial statements. Therefore, the transferee would not be a consolidated affiliate of the transferor, and such a transfer could isolate the transferred financial assets and be accounted for as a sale if all other conditions of paragraph 9 are met. [Revised 6/09.]

21. [Deleted 6/09 because Statement 140, as amended by Statement 166, amends the definition of proceeds to include beneficial interests.]

~~*Q*—If a transferor transfers assets to a trust and receives a note receivable (issued by a third-party investor) in exchange, assuming all of the conditions of paragraph 9 have been satisfied, would that note receivable represent proceeds from a sale or would it represent a beneficial interest in the transferred assets?~~

~~A—The answer depends on the nature of the note receivable. If the note receivable is a general obligation of the third-party investor, then it would represent proceeds from a sale. On the other hand, if the note receivable is solely collateralized by the assets in the trust without recourse to the third-party investor, then, in effect, the note represents a beneficial interest in the transferred assets that would preclude sale accounting pursuant to paragraph 9 to the extent of the beneficial interest retained.~~

Conditions That Constrain a Transferee

22. *Q*—Assuming that all of the other requirements of paragraph 9 are met, has a transferor surrendered control over transferred financial assets if the transferee ~~(that is not a qualifying special-purpose entity (SPE))~~ (that is not an entity whose sole purpose is to engage in securitization or asset-backed financing activities) is precluded from *exchanging* the transferred financial assets but obtains the unconstrained right to *pledge* them? [Revised 6/09.]

A—The answer depends on the facts and circumstances. In a transfer of financial assets, a transferee's right to both pledge and exchange transferred financial assets suggests that the transferor has surrendered its control ~~of~~ over those financial assets. However, more careful analysis is warranted if the transferee may only pledge the transferred financial assets. Paragraph 9(b) requires that the transferee have the right to pledge *or* exchange the transferred financial assets. The Board's reasoning for that condition is explained in paragraph 161, which states that the transferee has obtained control over the transferred assets if it can ~~sell~~ pledge or exchange the transferred assets and, thereby, "obtain all or most of the cash inflows that are the primary economic benefits of financial assets." As discussed in paragraphs 168 and 169, the Board concluded that the key concept is "the ability to obtain all or most of the cash inflows, *either* by exchanging the transferred asset *or* by pledging it as collateral" (paragraph 169). Also, paragraph 29A explains that transferor-imposed contractual constraints that narrowly limit timing or terms, for example, allowing a transferee to pledge only on the day assets are obtained or only on terms agreed to with the transferor, also constrain the transferee and presumptively provide the transferor with more-than-trivial benefits. [Revised 6/09.]

22A. *Q*—Assume an entity transfers financial assets to a transferee ~~an entity that is not a qualifying SPE. The transferee~~ that is significantly limited in its ability to pledge or exchange the transferred assets (the transferee is not an entity

[7]~~The phrase *consolidated affiliate of the transferor* is defined in paragraph 364 of Statement 140 as "an entity whose assets and liabilities are included with those of the transferor in the consolidated, combined, or other financial statements being presented."~~

[8]~~The transferor must still consider whether consolidation of the transferee is required under GAAP.~~

whose sole purpose is to engage in securitization or asset-backed financing activities). The transferor receives cash in return for the transferred financial assets and has *no* continuing involvement with the transferred financial assets~~—no servicing responsibilities, no participation in future cash flows, no recourse obligations other than standard representations and warranties that the financial assets transferred met the delivery requirements under the arrangements, no further involvement of any kind~~. Does the transfer meet the requirements of paragraph 9(b) of Statement 140? [Revised 6/09.]

A—Yes. For a transfer to fail to meet the requirements of paragraph 9(b), the transferee must be constrained from pledging or exchanging the transferred financial asset *and* the transferor must receive more than a trivial benefit as a result of the constraint. As noted in paragraph 166 of Statement 140, ". . . transferred financial assets from which the transferor can obtain no further benefits are no longer its assets and should be removed from its statement of financial position." [Revised 6/09.]

For transfers ~~to an entity that is not a qualifying SPE after~~ in which the transferor does have *any* continuing involvement, an evaluation must be made as to whether the requirements of paragraph 9(b), as explained by paragraphs 29–~~34~~ 33 of Statement 140, have been met. [Added 9/01~~.~~; revised 6/09.]

23. *Q*—In certain loan participation agreements involving transfers of participating interests, the transferor is required to approve any subsequent transfers or pledges of the interests in ~~portion of~~ the loans held by the transferee. Would that requirement be a constraint that would prevent the transferee from taking advantage of its right to pledge or to exchange the transferred financial asset and, therefore, preclude accounting for the transfer as a sale? [Revised 6/09.]

A—The answer depends on the nature of the requirement for approval. Sale accounting is precluded if conditions imposed by the transferor both constrain a transferee and provide more than a trivial benefit to the transferor. Paragraph 106 explains that ". . . if the loan participation agreement constrains the transferee~~s~~ from pledging or exchanging ~~their participations~~its participating interest and that constraint provides a more-than-trivial benefit to the transferor, ~~the transferor presumptively receives a more than trivial benefit,~~ the transferor has not relinquished control ~~over the loan,~~ and shall account for the transfer~~s~~ as a secured borrowing~~s~~." [Revised 6/09.]

Some transferor-imposed conditions do not constrain the transferee. Paragraph 30 states that "a transferor's right of first refusal on the occurrence of a bona fide offer to the transferee from a third party . . ."[9] or ". . . a requirement to obtain the transferor's permission to sell or pledge that is not to be unreasonably withheld" ~~does~~ may not presumptively constrain a transferee. A prohibition on sale to the transferor's competitor may or may not constrain a transferee from pledging or exchanging the financial asset, depending on how many other potential buyers exist. If there are many other potential willing buyers, the prohibition would not be constraining. In contrast, if that competitor were the only potential willing buyer (other than the transferor), then the condition would be constraining. [Revised 6/09.]

Judgment is necessary to determine whether a requirement to obtain the transferor's permission to sell or exchange should preclude sale accounting.

24. *Q*—If a ~~qualifying SPE~~ securitization entity issues beneficial interests in the form of Rule 144A securities and the holder of those beneficial interests may not transfer them unless an exemption from the 1933 U.S. Securities Act registration is available, do the limits on the transferability of the beneficial interests result in a constraint on the transferee's right to pledge or exchange those beneficial interests and, therefore, preclude sale accounting by the transferor? [Revised 6/09.]

A—Issuing beneficial interests in the form of Rule 144A securities presumptively would not constrain a transferee's ability to transfer those beneficial interests for purposes of Statement 140, as amended by Statement 166. The primary limitation imposed by Rule 144A is that a potential buyer must be a sophisticated investor. If a large number of qualified buyers exist, the holder could transfer those securities to many potential buyers and, thereby, realize the full economic benefit of the assets. In such circumstances, the requirements of Rule 144A would not be a constraint that precludes sale accounting under paragraph 9(b). [Revised 6/09.]

~~Qualifying Special-Purpose Entities~~

~~Limits on permitted activities~~

24A. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Is it permissible for another entity to perform activities on behalf of a qualifying special-purpose entity (SPE) or to direct the qualifying SPE to perform activities—that otherwise would not be permitted activities of the qualifying SPE?~~

~~*A*—No. The significant limitations on the activities of a qualifying SPE required by Statement 140 apply whether those activities are carried out by the qualifying SPE itself or by its agent or anyone else acting on its behalf. [Added 9/01.]~~

25. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Assume that the risk inherent in a commercial loan portfolio securitized through a qualifying SPE increases because of adverse changes in an industry for which a concentration of loans exists. Can the servicer, which may be the transferor, use discretion to select which loans to sell back to itself (or to a third party) at fair value in response to that increased risk or concentration?~~

~~*A*—No. A qualifying SPE's powers are restricted to those in paragraph 35 of Statement 140. A transferor's or servicer's having *discretion to select* which loans to remove to reposition a portfolio is beyond those powers set forth in paragraph 35(d)(1) of Statement 140. Sale accounting would also be precluded under the provisions of paragraphs 9(e)(2), 54, and 86(a) of Statement 140 because such a power gives the transferor the unilateral right to reclaim *specific* assets from the qualifying SPE.~~

25A. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Can a servicer of assets held by a qualifying SPE have discretion in disposing of defaulted loans? Is that ability consistent with the restriction on a qualifying SPE?~~

~~*A*—No. Paragraph 35(d)(1), as illustrated in paragraph 43(a) of Statement 140, specifically prohibiting qualifying SPE from having discretion in disposing of defaulted loans (or other financial assets). However, if the servicing agreement in effect at the time the SPE was established describes specific conditions in which a servicer of a defaulted loan is required to dispose of the loan and the servicer has no choice but to dispose of the defaulted loan when the described conditions occur, then such a loan disposal is a permitted activity of qualifying SPE. [Added 9/01.]~~

25B. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Some servicing agreements require the servicer to either dispose of or hold (work out or foreclose) defaulted nonrecourse loans secured by commercial real estate based on the result of a net present value (NPV) computation that is designed to maximize the return on the defaulted loan. Is the rule described in this question consistent with the requirements of paragraph 35(d)(1) of Statement 140?~~

~~*A*—No. To analyze a compound rule like that described in this question, all possible outcomes should be analyzed and each possible outcome must comply with paragraph 35(d)(1).~~

~~It is also necessary to consider the overall process involved when determining whether a rule is an automatic response. In many of the decision rules that could be formulated (including the example in the question), the value or other inputs must be estimated. Depending on the nature of the inputs and the sophistication of the judgment required to obtain or filter those inputs, a specific decision rule may not be automatic and therefore not meet the requirements of paragraph 35(d)(1). Indicators that such inputs are not automatic for the purposes of paragraph 35 include the need for the involvement of highly experienced personnel and the existence of provisions that permit other beneficial interest holder (BIHs) to review and challenge those inputs.~~

~~For example, the specific fact pattern referred to in this question, in which significant judgment is required to estimate the inputs to the computation, leads to the conclusion that the decision rule is not automatic. In that case, significant judgments are required in estimating future vacancy and rental rates, the projected timing and sale price of foreclosed property, and the terms of a workout arrangement still to be negotiated, all of which are input into the NPV model. [Added 9/01.]~~

~~***Derivative financial instruments***~~

26. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Can an SPE enter into certain types of derivative transactions at the time beneficial interests are issued and still be qualifying?~~

~~*A*—Yes, but only if those transactions (a) result in derivative financial instruments that are *passive* in nature and *pertain*[10] to beneficial interests issued or sold to entities other than the transferor, its affiliates, or its agents; (b) do not create conditions that violate the provisions of paragraphs 35(c)(2) and 35(d); and (c) provide in its legal documents the powers of the SPE to enter into derivative transactions. Refer to Questions 27 and 28.~~

~~To illustrate, a qualifying SPE is precluded from entering into written options that provide the holder with an opportunity to trigger a condition that enables the SPE to sell transferred assets under circumstances inconsistent with the requirements of paragraph 35(d)(2) of Statement 140.~~

~~If an SPE enters into certain derivative instruments, sale accounting is precluded, not because the SPE is not qualifying, but because other provisions of paragraph 9 have not been met. Examples of those instruments include:~~

- ~~Derivative instruments that preclude the transferor from achieving legal isolation under paragraph 9(a)~~
- ~~Derivative instruments through which the transferor retains effective control over the transferred assets under paragraph 9(c).~~

27. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Can an SPE be qualifying if it can enter into certain types of derivative transactions subsequent to the time that beneficial interests are issued?~~

~~*A*—Generally, no. As discussed in Question 26, a qualifying SPE can enter into derivative transactions at the time beneficial interests are issued under paragraph 35(c)(2) as interpreted by paragraphs 39 and 40. However, a derivative entered into by the qualifying SPE at the time beneficial interests were issued may only be *replaced* upon occurrence of a pre-specified event or circumstance outside the control of the transferor, its affiliates, or its agents (for example, a default by the derivative counterparty) *as specified in the legal documents that established the qualifying SPE*.~~

28. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Can an SPE be considered qualifying if it has the power to enter into a derivative contract that, in effect, would result in that SPE's selling assets with the primary objective of realizing a gain or maximizing return?~~

~~*A*—No. Paragraph 35(d)(1) (as interpreted by paragraphs 42 and 43) limits a qualifying SPE's ability to sell (or otherwise dispose of) noncash financial assets held by it to situations where there is, or is expected to be, a "*decline* by a specified degree *below* the fair value of those assets when the SPE obtained them" (emphasis added). Derivative instruments designed to effectively realize gains would be inconsistent with this provision. Refer to Questions 26 and 27.~~

~~***Servicing activities***~~

28A. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Sometimes, a servicer or other BIH in a qualifying SPE retains the right (an option) to~~

~~[10]The meanings of *passive* and *pertain* with respect to derivative financial instruments are discussed in paragraphs 39 and 40.~~

~~purchase defaulted loans (that is, through physical settlement—in some cases for a fixed amount and in other cases at fair value). Are such options consistent with the restrictions on a qualifying SPE?~~

~~*A*—Yes. If the party holding the default call option is the transferor (or its affiliates or its agents), the option is a default removal-of-accounts provision (ROAP) or other physically settled contingent call option that is specifically permitted by paragraph 35(d)(3) of Statement 140. The determination of how that kind of option affects the accounting by the transferor is complex, and it is necessary to consider the overall effect of related rights and obligations in making that assessment. See Question 49 for guidance on how the transferor is affected by such options.~~

~~If a party other than the transferor, its affiliates, or its agents holds the default call option, that right is a beneficial interest. Paragraph 44(a) of Statement 140 permits a qualifying SPE to dispose of assets in response to a BIH (other than the transferor, its affiliates, or its agents) exercising its right to put its beneficial interest back to the qualifying SPE in exchange for a full or partial distribution of the assets held by the qualifying SPE. The fact that the holder of the option must also pay cash (equal to the option's exercise price, which may be the fair value of the underlying financial instrument) in the exchange should not result in a different conclusion in applying paragraph 44(a). [Added 9/01.]~~

28B. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—When a loan becomes delinquent or defaults, the servicer typically attempts to restructure or "work out" the loan in lieu of foreclosing on the collateral. Is the discretion permitted a servicer to work out a loan consistent with the limited powers permitted a qualifying SPE?~~

~~*A*—Yes. A servicer may have discretion in restructuring or working out a loan as long as that discretion is significantly limited and the parameters of that discretion are fully described in the legal documents that established the qualifying SPE or that created the beneficial interests in the transferred assets. However, the servicer may not initiate new lending to the borrower through the qualifying SPE as a result of the workout. (Refer to paragraph 185 of Statement 140.) Examples of activities that are not new lending are:~~

- ~~Payments made by a servicer after a debtor fails to pay them (for example, to pay delinquent property taxes, to ensure required property and casualty insurance coverage is maintained, and so forth) that are contemplated in the lending agreement prior to its transfer to the qualifying SPE.~~
- ~~Advances of funds by servicers (whether required or discretionary) to facilitate timely payments to the beneficial interest holders, after which the servicer has a priority right to recoup its advances from future cash inflows. That activity does not represent new lending activity to the borrower because it does not increase the indebtedness of the borrower.~~
- ~~Extension of further credit by a transferor in a credit card securitization or revolving-period securitization and the subsequent transfer of the resulting loan by the transferor to qualifying SPE, pursuant to agreements in the legal documents that established the qualifying SPE. That is not a new lending activity *by a qualifying SPE* because the loan is originated by the transferor, not through the qualifying SPE. [Added 9/01.]~~

28C. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Is the decision to initiate foreclosure activities a servicing activity or a disposal of a loan?~~

~~*A*—It is a servicing activity. Foreclosure is a means by which the servicer attempts to collect principal and interest due on a loan. It is not a loan disposal. A servicer may have discretion in determining when to initiate foreclosure proceedings as long as that discretion is significantly limited and the parameters of that discretion are fully described in the legal documents that established the qualifying SPE or that created the beneficial interests in the transferred assets. [Added 9/01.]~~

28D. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—May a servicer of assets held by a qualifying SPE have some discretion in managing and disposing of foreclosed assets?~~

~~*A*—Yes. A servicer may have discretion to dispose of foreclosed assets that it temporarily holds (as long as that discretion is significantly limited and the parameters of that discretion are fully described in the legal documents that established the qualifying SPE or that created the beneficial interests in the transferred assets).~~

~~However, certain activities that could be undertaken by a servicer managing foreclosed assets are inconsistent with the discretion permitted a qualifying SPE because they are inconsistent with the provisions of paragraphs 35 and 37 of Statement 140. Judgment needs to be applied to determine whether a specific activity is inconsistent with those provisions.~~

29. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Can an SPE that is permitted to hold title to nonfinancial assets *temporarily* as a result of foreclosing on financial assets be considered qualifying?~~

~~*A*—Yes. Holding servicing rights to financial assets that it holds is a permitted activity for qualifying SPEs under paragraph 35(c)(5) (as interpreted by paragraph 41). Paragraph 61 indicates that servicing includes executing foreclosure if necessary. Therefore, an SPE that holds title to nonfinancial assets *temporarily* as a result of executing foreclosure on financial assets in connection with servicing can be considered qualifying. [Refer to Question 28A.] [Revised 9/01.]~~

~~***Limits on what a qualifying SPE may hold***~~

30. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Can an SPE that holds an investment accounted for under the equity method be qualifying?~~

~~*A*—Generally not. Entities account for an investment in accordance with the equity method if they have the ability to exercise *significant influence* over that investment as described by paragraph 17 of APB Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock.* Qualifying SPEs are limited to holding passive investments in financial assets. Paragraph 39 of Statement 140 notes that "investments are not passive if through them . . . the SPE or any related entity . . . is able to exercise control or *significant influence* . . ." (emphasis added). However, that limitation does not apply to certain investments that are accounted for (for example, under EITF Topic No. D-46, "Accounting for Limited Partnership Investments") in accordance with the equity method, even though the investor does not have the ability to exercise significant influence. Refer to Question 41.~~

Unilateral rights held by the transferor

31. *Q*—Credit card securitizations often include a "removal-of-accounts" provision (ROAP) that permits the seller, under certain conditions and with trustee approval, to withdraw receivables from the pool of securitized receivables. Does a transferor's right to remove receivables from a credit card securitization preclude accounting for a transfer as a sale?

A—It depends on the rights that the transferor has under the ROAP. A ROAP that does not allow the transferor to unilaterally reclaim specific financial assets from the ~~qualifying SPE~~ transferee, as described in paragraphs ~~35(d)(3), 51–~~ 50–54, ~~and~~ 87, and 88, does not preclude sale accounting. Paragraphs 86 and 88 provide~~s~~ examples of ROAPs that would allow the transferor to unilaterally reclaim specific transferred financial assets and preclude sale accounting under paragraph 9(c). Refer to Question 49. [Revised 6/09.]

32. *Q*—~~If a transferor's retention of beneficial interests in financial assets transferred to a nonqualifying SPE that cannot pledge or exchange its assets permits the transferor~~ If a transferor has the ability to dissolve ~~the SPE~~ a securitization entity (for example, through the beneficial interests that it holds) and reassume control of the transferred financial assets at any time, is the transferor precluded from accounting for the transfer as a sale? [Revised 6/09.]

A—Yes.~~, for two reasons. First, because the SPE cannot pledge or exchange the assets (it is not a qualifying SPE) and this restriction provides the transferor with the more than trivial benefit of knowing that the assets (which it is entitled to reacquire) must remain in the SPE, sale accounting is precluded under paragraph 9(b).~~

~~Second, the~~The transferor's current ability to dissolve the securitization entity ~~SPE~~ and reassume control of the transferred financial assets entitles it to unilaterally cause the return of the transferred financial assets, ~~which~~ indicating that the transferor has maintained effective control over the transferred financial assets, which would preclude~~s~~ sale accounting under paragraph 9(c)~~(2)~~. [Revised 6/09.]

~~***Beneficial interests***~~

33. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Can a fixed-maturity debt instrument, a commercial paper obligation, or an equity interest be considered a beneficial interest in a qualifying SPE?~~

~~*A*—Yes. Paragraph 75 states that ". . . beneficial interests may comprise either a single class having equity characteristics or multiple classes of interests, some having debt characteristics and others having equity characteristics." Paragraph 173 explains that:~~

> ~~Qualifying SPEs issue beneficial interests of various kinds—variously characterized as debt, participations, residual interests, and otherwise—as required by the provisions of those agreements.~~

34. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Can a qualifying SPE "assume" the obligations of a transferor or the obligations of some other entity?~~

~~*A*—While assuming the debt of another entity is not specifically among the permitted activities of a qualifying SPE as described in paragraph 35, an SPE can issue beneficial interests, including those in the form of debt securities or equity securities, and be considered *qualifying*. Paragraph 364 defines *beneficial interests* as:~~

> ~~Rights to receive all or portions of specified cash inflows to a trust or other entity, including senior and subordinated shares of interest, principal, or other cash inflows to be "passed-through" or "paid-through," premiums due to guarantors, commercial paper obligations, and residual interests, whether in the form of debt or equity.~~

~~If a lender legally releases the transferor from being the primary obligor under a liability assumed by an SPE, the lender is, in fact, accepting a beneficial interest in the assets held by that SPE in exchange for the loan it previously held. Therefore, a qualifying SPE can issue beneficial interests in the transferred financial assets that it holds to a lender and, in effect, assume or "incur" a debt obligation. An example of such an assumption by a qualifying SPE is found in Question 35.~~

35. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—May a debtor derecognize a liability (without having to recognize another, similar liability) if it transfers noncash financial assets to a qualifying SPE that "assumes" the liability?~~

~~*A*—Yes, but only if the liability is considered extinguished under paragraph 16 and the transfer of the noncash financial assets is accounted for as a sale under paragraph 9.~~

~~A debtor may derecognize a liability if and only if it has been extinguished. Paragraph 16 states that a liability has been extinguished if either of the following two conditions is met:~~

- ~~The debtor pays the creditor and is relieved of its obligation for the liability.~~
- ~~The debtor is legally released from being the primary obligor under the liability, either judicially or by the creditor.~~

~~The transfer of assets to a qualifying SPE would not, in most cases, constitute a payment to the creditor and, therefore, would not meet~~

~~the condition in paragraph 16(a) of Statement 140. However, the debtor may extinguish its liability if, as a result of transferring the assets to the qualifying SPE, the debtor is legally released from being the primary obligor under the liability according to paragraph 16(b) of Statement 140. If the creditor's legal release is not obtained, the debtor should continue to recognize the obligation.~~

~~A debtor that is legally released from being the primary obligor by the transfer of noncash financial assets may, nevertheless, be required to recognize another, similar liability if it continues to recognize those noncash financial assets that were transferred to the qualifying SPE. According to the provisions of paragraph 12 of Statement 140:~~

> ~~If a transfer of financial assets in exchange for cash or other consideration (other than beneficial interests in the transferred assets) does not meet the criteria for a sale in paragraph 9, the transferor and transferee shall account for the transfer as a secured borrowing with pledge of collateral (paragraph 15).~~

~~If all of the conditions of paragraph 9 are not met for the transfer of noncash financial assets to the SPE (for example, because the SPE is not *qualifying* and the provisions of paragraph 9(b) are not met), the entity will continue to recognize those assets. That also will result in the entity's recording an obligation to pass through the cash flows from those transferred assets to the qualifying SPE.~~

~~Consolidated financial statements~~

36. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Can a qualifying SPE simultaneously be a conduit for separate (that is, no commingling or cross-collateralization) securitizations from more than one transferor? In other words, can a "condominium structure" be a qualifying SPE?~~

~~*A*—Yes, as long as the restrictive criteria of paragraph 35 are met. That guidance does not prohibit a qualifying SPE from acting as a conduit for more than one securitization transaction, even if the individual "condominiums" (which are sometimes referred to as "silos") hold dissimilar financial assets. If a qualifying SPE serves as a conduit for different transferors, each condominium is effectively a qualifying SPE. Therefore, each transferor applies the consolidation guidance in paragraph 46 of Statement 140 to its condominium. Refer to Question 60.~~

37. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Should a qualifying SPE be consolidated by the transferor or its affiliates?~~

~~*A*—No. Paragraph 46 states that "a qualifying SPE shall not be consolidated in the financial statements of a *transferor or its affiliates*" (emphasis added).~~

~~Paragraph 25 of Statement 140 permits a formerly qualifying SPE that fails to meet one or more conditions for being a qualifying SPE to be considered a qualifying SPE if it maintains its qualifying status under previous accounting standards, does not issue new beneficial interests after the effective date, and does not receive assets it was not committed to receive before the effective date. Otherwise, a formerly qualifying SPE and assets transferred to it shall be subject to other consolidation policy standards and guidance, and to all provisions of Statement 140.~~

~~Beneficial interest holders, sponsors, servicers, and others involved with a qualifying SPE that are not affiliated with the transferor should apply Interpretation 46 to determine whether they should consolidate a qualifying SPE if they meet the requirements in paragraph 4(d) of Interpretation 46. [Revised 4/03.]~~

38. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Should a transferor apply Statement 140's consolidation provisions when determining whether to consolidate a qualifying SPE if some or all of the transfers of financial assets to that SPE are accounted for as secured borrowings under paragraph 9?~~

~~*A*—Yes. The conditions for sale accounting in paragraph 9 are irrelevant to determining whether a transferee is a qualifying SPE and whether it should be consolidated.~~

~~The result of applying Statement 140 if financial assets are transferred to a qualifying SPE in transactions that were accounted for by the transferor as secured borrowings is that the qualifying SPE would not be consolidated by the transferor and the assets transferred to the qualifying SPE would continue to be recognized by the transferor because the conditions for sale accounting have not been met.~~

39. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—If a transferor subsequently transfers all the equity interests in a previously unconsolidated qualifying SPE to an unrelated third party, would that third party be able to use Statement 140 as its basis for evaluating consolidation accounting?~~

~~*A*—No. Paragraph 46 of Statement 140 is limited to consolidation by the "transferor or its affiliates." If that third party "has the unilateral ability to cause the entity to liquidate or to change the entity so that it no longer meets the conditions in paragraph 25 or 35 of Statement 140," the requirements of Interpretation 46 apply. [Revised 4/03.]~~

40. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Assume that an entity transfers financial assets to a qualifying SPE in a transaction that meets the criteria for sale accounting. Should the transferor consolidate the qualifying SPE if it retains more than 50 percent of the fair value of the beneficial interests issued by the qualifying SPE?~~

~~*A*—No. Paragraph 46 provides that "a qualifying SPE shall not be consolidated in the financial statements of a transferor or its affiliates." That provision does not make a distinction based on the proportion of the qualifying SPE's beneficial interests that are retained by the transferor. However, paragraph 36 provides that if the transferor holds more than 90 percent of the fair value of the beneficial interests, that would preclude the SPE from being a qualifying SPE unless the transfer is a guaranteed mortgage securitization.~~

41. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.]

~~*Q*—Assume that Company A holds a 30 percent ownership interest in Company B. Company A sells 5 percent of that interest in Company B to an SPE, thereby reducing its interest to 25 percent. Before and after the transfer, Company A accounts for its ownership interest in Company B under the equity method. Use of the equity method under Opinion 18 presumes that Company A has significant influence over Company B. Under Statement 140, Company A cannot be a qualifying SPE if it holds investments that allow it or others to exercise control or *significant influence* over the investee. Would Company A be precluded from applying the consolidation guidance in Statement 140 to that SPE? Would it make a difference if Company A's ownership interest in Company B is reduced to a level such that the investment is no longer accounted for under the equity method after the transfer?~~

~~*A*—Yes and perhaps, respectively.~~

~~Yes, Company A is precluded from applying the consolidation guidance in Statement 140 to that SPE because the SPE is not a qualifying SPE. A qualifying SPE may hold only passive instruments. Paragraph 39 explains that:~~

> ~~Investments are not passive if through them, either in themselves or in combination with other investments or rights, the SPE or any related entity, such as the transferor, its affiliates, or its agents, is able to exercise control or significant influence . . . over the investee.~~

~~However, if as a result of the transfer, the transferor, the SPE, and any other related entities in combination cannot exercise significant influence or control over the investee, and the SPE meets the other requirements of Statement 140 to be a qualifying SPE, the transferor would apply the consolidation provision of paragraph 46. Refer to Question 30.~~

Effective Control

42. *Q*—Dollar-roll repurchase agreements (also called dollar rolls) are agreements to sell and repurchase similar but not identical securities. Dollar rolls differ from regular repurchase agreements in that the securities sold and repurchased, which are usually of the same issuer, are represented by different certificates, are collateralized by different but similar mortgage pools (for example, conforming single-family residential mortgages), and generally have different principal amounts. Is a transfer of financial assets under a dollar-roll repurchase agreement within the scope of Statement 140?

    A—A transfer of financial assets under a dollar-roll repurchase agreement is within the scope of Statement 140 if that agreement arises in connection with a transfer of existing securities.[11] In contrast, dollar-roll repurchase agreements for which the underlying securities being sold do not yet exist or are to be announced (for example, TBA GNMA rolls) are outside the scope of Statement 140 because those transactions do not arise in connection with a transfer of recognized financial assets. In those cases, other existing literature should be applied. For example, the provisions of Statement 133 or EITF Issue No. 84-20, "GNMA Dollar Rolls," may apply to what are considered Type 4 securities by that Issue. Any type of Type 4 contracts that are not subject to Statement 133's provisions must be marked to market as required by Issue 84-20.

43. *Q*—Does paragraph 9(c)~~(1)~~ preclude sale accounting for a dollar-roll transaction that is subject to the provisions of Statement 140? [Revised 6/09.]

    A—The answer depends on the facts and circumstances. For example, paragraph 9(c)(1) describes an example of effective control that is further explained in~~to preclude sale accounting, pursuant to~~ paragraph 47~~(a),~~. Paragraph 47(a) requires that "the financial assets to be repurchased or redeemed are ~~[must be]~~ the same or substantially the same as those transferred. . . ." Paragraph 48 describes six characteristics that must *all* exist ~~in order~~ for a transfer to meet the substantially-the-same requirement in paragraph 47(a). One of those characteristics is that the same aggregate unpaid principal amount or principal amounts within accepted "good-delivery" standards for the type of security involved must be met. However, the good-delivery standard is only one of the six characteristics that must exist. Another is that the transferor must be able to repurchase or redeem the transferred financial assets on substantially the agreed terms, even in default by the transferee. Refer to Question 45. [Revised 6/09.]

44. *Q*—In a transfer of existing securities under a dollar-roll repurchase agreement, if the transferee is committed to return substantially-the-same securities to the transferor but that transferee's securities were TBA (to be announced) at the time of transfer, would the transferor be precluded from accounting for the transfer as a secured borrowing?

    A—No. For transfers of existing securities under a dollar-roll repurchase agreement, the transferee must be committed to return substantially-the-same securities to the transferor~~ to fail the condition in paragraph 9(c)(1) that would preclude sale accounting.~~, which would indicate that the transferor has maintained effective control. The financial asset to be returned may be TBA at the time of the transfer because the transferor would have no way of knowing whether the transferee held the security to be returned. That is, the transferor is only required to obtain a commitment from the transferee to return substantially-the-same securities and is not required to determine that the transferee holds the securities that it has committed to return. [Revised 6/09.]

45. *Q*—Paragraph 49 states that "to be able to repurchase or redeem financial assets on substantially the agreed terms, even in the event of default by the transferee, a transferor must at all times during the contract term have obtained cash or other collateral sufficient to fund substantially all of the cost of purchasing replacement financial assets from others." Would ~~the requirement of paragraph 9(c)(1) preclude sale accounting by the transferor~~ a transferor maintain effective control if, under the arrangement,

[11] If the dollar-roll repurchase agreement is accounted for as a sale under Statement 140, Statement 133 provides guidance on the subsequent accounting for the forward contract.

the transferor is substantially overcollateralized at the date of transfer even though the arrangement does not provide for frequent adjustments to the amount of collateral maintained by the transferor? [Revised 6/09.]

A—No. A mechanism to ensure that adequate collateral is maintained must exist even in transactions that are substantially overcollateralized (for example, "deep discount" and "haircut" transactions) for paragraph 9(c)~~(1)~~ to indicate that the transferor has maintained effective control that would preclude sale accounting for those transactions~~,. Even~~ even if the probability of ever holding inadequate collateral appears remote~~,~~. ~~as~~As explained in paragraph 49~~, the requirement of paragraph 9(c)(1) would *not* be met and sale accounting by~~ the transferor would not maintain effective control ~~be precluded~~ unless the arrangement assures, by contract or custom, that the collateral is sufficient "at all times . . . to fund substantially all of the cost of purchasing replacement financial assets from others." [Revised 6/09.]

Statement 140 does not prescribe that a specific contractual term, such as a margining provision, must be present to meet the sufficient collateral requirement. Instead, Statement 140 prescribes, as explained in paragraph 218, what the effect of the arrangement must be—that the transferor "is protected by obtaining collateral sufficient to fund substantially all of the cost of purchasing identical replacement securities during the term of the contract so that it has received the means to replace the assets even if the transferee defaults." Simply excluding a margining provision from a repurchase agreement does not change the accounting that results if the maintenance of sufficient collateral is otherwise assured. For example, a contractual provision that a repurchase agreement is immediately terminated should the value of the collateral become insufficient to fund substantially all of the cost of purchasing replacement financial assets would satisfy the requirement in paragraph 49. [Revised 6/09.]

46. *Q*—Paragraph 49 requires that ". . . a transferor must at all times during the contract term have obtained cash or other collateral sufficient to fund *substantially all* of the cost of purchasing replacement financial assets from others" (emphasis added). *Substantially all* is not specifically defined in Statement 140. Should entities ~~analogize to APB Opinion No. 16, *Business Combinations,* and~~ interpret *substantially all* to mean 90 percent or more? [Revised 6/09.]

A—No. The Board elected not to define *substantially all* because, as explained in paragraph 218, "judgment is needed to interpret the term *substantially all* and other aspects of the criterion that the terms of a repurchase agreement do not maintain effective control over the transferred asset." Paragraph 218 further states:

> . . . arrangements to repurchase or lend readily obtainable securities, typically with as much as 98 percent collateralization (for entities agreeing to repurchase) or as little as 102 percent overcollateralization (for securities lenders), valued daily and adjusted up or down frequently for changes in the market price of the security transferred and with clear powers to use that collateral quickly in the event of default, typically fall clearly within that guideline. The Board believes that other collateral arrangements typically fall well outside that guideline.

Judgment should be applied based on the facts and circumstances.

47. *Q*—Does Statement 140 contain *special provisions* for differences in collateral maintenance requirements that exist in markets outside the United States?

A—No. The general provisions of Statement 140 apply. Market practices and contracts for repurchase, sale-buy backs, and securities lending transactions can vary significantly from market to market and country to country. ~~However, sale accounting is precluded by p~~Paragraph 9(c)(1) describes an example of effective control ~~only~~ if the transfer involves an agreement that both entitles and obligates the transferor to repurchase or redeem the transferred financial assets before maturity and all of the requirements of paragraphs 47–49 are met. [Revised 6/09.]

For example, in certain markets, it is not customary to provide or maintain collateral in connection with repurchase transactions. In addition, in ~~emerging market~~ certain repurchase agreements, the amount of cash lent often is limited to an amount substantially less than 100 percent (for example, 80 percent or less) of the value of the securities transferred under the repurchase agreements because of the level of market and credit risk associated with those transactions. Statement 140 does not provide special provisions for those differences in collateral requirements~~ and, as a result, sale accounting would not be precluded by paragraph 9(c)(1) for those transactions~~. [Revised 6/09.]

48. *Q*—The example of effective control in ~~P~~paragraph 9(c)(1) of Statement 140 states that the transferor maintains effective ~~a transferor has surrendered~~ control over the transferred financial assets ~~if it does not maintain effective control over the transferred assets~~ through "an agreement that both entitles and obligates the transferor to repurchase or redeem them *before their maturity* . . ." (emphasis added). What does the term *before maturity* mean in the context of the transferor maintaining effective control under the provisions of Statement 140? [Revised 6/09.]

A—Statement 140 does not specifically define the term *before maturity.* However, in describing whether a transferor maintains effective control over transferred financial assets through a right and obligation to repurchase, paragraph 213 states that ". . . the Board concluded that the only meaningful distinction based on required repurchase at some proportion of the life of the assets transferred is between a 'repo-to-maturity,' in which the typical settlement is a net cash payment, and a repurchase before maturity, in which the portion of the asset that remains outstanding is indeed reacquired in an exchange." A transferor's agreement to repurchase a transferred financial asset would not be considered a repurchase or redemption before maturity if, because of the timing of the redemption, the transferor would be unable to sell the financial asset again before its maturity (that is, the period until maturity is so short that the typical settlement is a net cash payment). [Revised 6/09.]

49. *Q*—How do different types of rights of a transferor to reacquire (call) transferred financial assets affect sale accounting under Statement 140? [Revised 6/09.]

A—Sale accounting is precluded if a transferor's right to reacquire (call) a transferred financial asset[12] ~~has any of three effects:~~ constrains the ability of a transferee (or, if the transferee is an entity whose sole purpose is to engage in securitization or asset-backed financing activities and that entity is constrained from pledging or exchanging the assets it receives, each third-party holder of its beneficial interests) to pledge or exchange the transferred financial assets (or beneficial interests) it received and provides more than a trivial benefit to the transferor (paragraph 9(b)). [Revised 6/09.]

In addition, paragraph 9(c) precludes sale accounting if a transferor, its consolidated affiliates included in the financial statements being presented, or its agents, maintain effective control over transferred financial assets. For example, sale accounting is precluded if a right to reacquire (call) a transferred financial asset has either of the following effects:

1. The transferor, its consolidated affiliates included in the financial statements being presented, or its agents, maintain effective control through an agreement that both entitles and obligates the transferor to repurchase or redeem the transferred financial asset before its maturity (paragraph 9(c)(1)); or~~A condition both constrains the transferee from taking advantage of its right to pledge or exchange the transferred asset(s) and provides more than a trivial benefit to the transferor (paragraph 9(b)).~~
2. The transferor, its consolidated affiliates included in the financial statements being presented, or its agents, maintain~~s~~ effective control through an agreement that ~~both entitles and obligates it to redeem transferred asset(s) before their maturity (paragraph 9(c)(1))~~ provides the transferor with both the unilateral ability to cause the holder

[12]All call options discussed in this question are or can be *physically settled.* Cash-settled call "options" do not constrain the transferee, nor do they result in the transferor maintaining effective control because they do not provide the transferor with an opportunity to reclaim the transferred financial assets. ~~(Certain cash-settled options may, however, be incompatible with the conditions that a qualifying SPE must meet.)~~ [Revised 6/09.]

to return the specific transferred financial assets and a more-than-trivial benefit attributable to that ability, other than through a cleanup call (paragraph 9(c)(2)).

~~3. The transferor maintains effective control through the ability to cause, unilaterally, the return of specific transferred assets (paragraph 9(c)(2)).[13]~~

A unilateral right to reclaim specific transferred financial assets permits a transferor to maintain effective control and precludes sale accounting ~~only for transferred assets that~~ if the transferor has the unilateral right to reacquire the transferred financial assets and if that right provides the transferor with more than a trivial benefit. Paragraph ~~52~~ 50 states that ~~clearly:~~ "~~. . .~~ a call or other right conveys more than a trivial benefit if the price to be paid is fixed, determinable, or otherwise potentially advantageous, unless because that price is so far out of the money or for other reasons it is probable when the option is written that the transferor will not exercise it." ~~on specific assets transferred to a qualifying SPE . . . maintains that transferor's effective control over the assets *subject to that call*" (emphasis added). Further, a right to reclaim specific transferred assets precludes sale accounting only if the transferor can exercise the right *unilaterally*. The following table summarizes Statement 140's provisions for different types of rights of a transferor to reacquire (call) transferred assets, including references to paragraphs in the Statement that provide more detail.~~ [Revised 6/09.]

~~[13]Statement 140 provides three exceptions under which the ability to cause, unilaterally, the return of specific transferred assets does not maintain effective control: cleanup calls, calls at fair value with no residual interest, and conditional calls.~~

~~Effective Control over Transferred Asset(s) through an Option or Repurchase Agreement~~

~~Transferor holds . . .~~	**~~Non-QSPE~~**	**~~QSPE~~**
	~~Unconditional Attached Call [¶364] (fixed price)~~ *	
~~–on all transferred assets~~	~~No sale. [¶9(c)(2)]~~	
~~–on a portion of the assets and:~~		
~~—can choose assets~~	~~No sale on covered assets. [¶9(c)(2); ¶52; ¶86(a)]~~	
~~—cannot choose assets~~†	~~Sale of part of the asset(s). [¶9(c)(2); ¶52; ¶87(a)]~~	
	~~Unconditional Embedded Call [¶364] (fixed price)~~*	
~~–in assets (embedded by issuer)~~	~~Does not preclude sale. [¶50]~~	
~~–in QSPE beneficial interests (embedded by QSPE)~~	~~Not applicable.~~	~~Effectively an attached call. [¶51] Analyze under those provisions.~~
	~~Unconditional Freestanding Call [¶364] (fixed price)~~*	
~~–on assets readily obtainable~~	~~Does not preclude sale. [¶9(b); ¶9(c)(2); ¶32]~~	~~Effectively an attached call. [¶51] Analyze under those provisions.~~
~~–on assets not readily obtainable~~	~~No sale. [¶9(b); ¶32]~~	~~Effectively an attached call. [¶51] Analyze under those provisions.~~
	~~ROAPs~~*	
~~–unconditional~~	~~Analyze as if it were either an attached or freestanding unconditional call.~~	
~~–conditional~~‡	~~Reanalyze as an unconditional call when the condition is resolved.~~	
	~~Exceptions~~	
~~Cleanup call~~	~~Does not preclude sale. [¶9(c)(2); ¶364]~~	
~~Fair value call (no residual interest)~~	~~Does not preclude sale unless it constrains the transferee. [¶9(c)(2); ¶52; ¶53]~~	
~~Conditional call~~	~~Does not preclude sale. Reanalyze provision when condition resolved.~~	
	~~Other Rights to Reclaim Assets~~	
~~Forward purchase agreement:~~		
~~—with collateral maintenance, etc.~~	~~No sale. [¶9(c)(1); ¶47–49]~~	
~~—without collateral maintenance~~	~~Analyze as either an attached or freestanding call. [¶9(c)(2)]~~	
~~Auction where transferor holds residual~~	~~Analyze as either an attached or freestanding call. [¶9(c)(2); ¶53]~~	
~~Right of first refusal~~§	~~Reanalyze as an unconditional call when the condition is resolved. [¶30]~~	

* ~~Unless the call is so far out of the money or for other reasons it is probable when the option is written that the transferor will not exercise it.~~

† ~~Some attached call options become exercisable (1) when the balance of the transferred pool or asset remaining reaches a specified level or (2) at a specified date. Possible credit losses or prepayments may make uncertain (a) the time until the option is exercisable or (b) the proportion of the pool or asset that will then remain, respectively. If such an option maintains the transferor's effective control over a portion of the transferred assets, the portion of the transferred assets to be derecognized and retained should be based on the relative fair values of (a) cash flows expected to be distributed to third party beneficial interest holders before the option becomes exercisable and (b) the balance of future cash flows expected to remain when the option becomes exercisable.~~

‡ ~~Conditional ROAPs are rights to reclaim assets that the transferor does not have the unilateral right to exercise.~~

§ ~~Unless the transferor can trigger activation of the right (see footnote 15 of Statement 140). In that case, the right should be analyzed as an in-substance call option.~~

Examples of Application of Effective Control Principles to ROAPs

- An unconditional ROAP that allows the transferor to specify the financial assets that may be removed from a group of financial assets precludes sale accounting for all financial assets in the group that might be specified~~,~~ if ~~because~~ such a provision allows the transferor unilaterally to remove specific financial assets and provides a more-than-trivial benefit to the transferor (paragraph 86(a)). That applies even if the transferor's right to remove specific financial assets from a group ~~pool~~ of transferred financial assets is limited, say, to 10 percent of the fair value of the financial assets transferred and all of the financial assets are smaller than that 10 percent: *none* of the transferred financial assets would be derecognized at the time of transfer because no transferred financial asset is beyond the reach of the transferor. If the transferor reclaims all the financial assets it can and thereby extinguishes its option, its control has expired and the rest of the financial assets have been sold at that time. [Revised 6/09.]
- A ROAP ~~for random removal of excess assets~~ that provides the right to random removal of excess financial assets from a group ~~pool~~ of transferred financial assets up to 10 percent of the fair value of the financial assets transferred (all financial assets in the group ~~pool~~ are ~~smaller~~ less than ~~this~~ 10 percent of the fair value of transferred financial assets) does not preclude sale accounting if the~~. The~~ transferor has no other interest in the group~~pool~~. The transferor has, in essence, obtained ~~retained~~ a 10 percent beneficial interest in the group ~~pool~~ and should account for it as such. This treatment is permitted because the ROAP is sufficiently limited and the transferor cannot unilaterally remove specific transferred financial assets, because the timing of the removal (when the excess develops) and the assets being removed (which are randomly determined) are not under the control of the transferor (see paragraph 87(a)). [Revised 6/09.]
- A ROAP conditioned on a transferor's decision to exit some portion of its business precludes sale accounting for all financial assets that might be affected, because it permits the transferor unilaterally to remove specific financial assets and provides a more-than-trivial-benefit to the transferor (paragraph 86(b)). [Revised 6/09.]
- A ROAP for defaulted receivables does not preclude sale accounting at the time of transfer, because the removal would be allowed only after a third party's action (default) and could not be caused unilaterally by the transferor (paragraph 87(b)). Once the default has occurred, the transferor would have the unilateral ability to remove those specific financial assets and would need to recognize the defaulted receivable if that ability provides a more-than-trivial-benefit to the transferor. [Revised 6/09.]
- A ROAP conditioned on a third-party cancellation, or expiration without renewal, of an affinity or private-label arrangement does not preclude sale accounting at the time of transfer because the removal would be allowed only after a third party's action (cancellation) or decision not to act (expiration) and could not be caused unilaterally by the transferor (paragraph 87(c)). Once the cancellation or expiration has occurred, the transferor would have the unilateral ability to remove specific financial assets and would need to recognize those financial assets if that ability provides a more-than-trivial-benefit to the transferor. [Revised 6/09.]

Other Examples of Application of Effective Control Principles

- In a loan participation, the lead bank (that is also the transferor) allows the participating bank to resell but reserves the right to call at any time from whoever holds it and can enforce the call by cutting off the flow of interest at the call date; such a call precludes sale accounting.
- In a securitization, a~~A~~ call permits the transferor to reclaim all of the transferred financial assets from the securitization entity~~qualifying SPE~~ at any time; such a call precludes sale accounting unless it is a fair value call on a readily obtainable asset in the marketplace and the transferor does not hold a residual beneficial interest in the transferred financial assets (see paragraph 53). [Revised 6/09.]
- A transferor-servicer transfers a group of entire financial assets to a securitization entity and has the right to call all of the financial assets ~~in the pool~~ when the group ~~it~~ amortizes to 20 percent of its value (determined at the date of transfer). The transferor-servicer determines that at that level of financial assets, its cost of servicing them would not be burdensome in relation to the benefits of servicing, and therefore that the call is not a cleanup call (paragraph 364). Such a call precludes sale accounting for the entire group of transferred financial assets (see Question 50).~~The~~

~~transferor-servicer has retained a 20 percent subordinated interest in the pool and should account for it as such.~~ [Revised 6/09.]

- If the third-party beneficial interests contain an embedded option and the transferor holds the residual interest in the ~~qualifying SPE~~securitization entity, the combination has the same kind of effective control as a scheduled auction provision if the transferor holds a residual beneficial interest (~~refer to~~ see paragraph 53). Sale accounting would be precluded for all of the transferred financial assets affected by the call~~or, if only part of the assets will remain when the option can be exercised, for the portion that would be subject to the call~~. [Revised 6/09.]
- If the third-party beneficial interests in a ~~qualifying SPE~~ securitization entity pay off first (a so-called turbo structure, where principal payments and prepayments are allocated on a non–pro rata basis), th~~e transfer could be viewed as meeting the requirements of paragraph 50~~ transferor may not maintain effective control over the transferred financial assets (see paragraph 52). To some extent, these repayments are contractual cash flows of the underlying assets, but repayments also result from prepayments in the underlying assets (that is, the prepayment options in the underlying assets are mirrored in the third-party beneficial interests). In this case, call options embedded in the third-party beneficial interests result from the options embedded in the underlying assets (that is, they are held by the underlying borrowers rather than the transferor), and thus do not preclude sale accounting~~ to the extent of the third-party interests~~. [Revised 6/09.]

50. *Q*—In certain transactions, the transferor is entitled to repurchase a transferred amortizing, individual (specific) financial asset when its remaining principal balance reaches some specified amount, for example, 30 percent of the original balance. To exercise that call, the transferor would pay the remaining principal balance. Under Statement 140, is such a transfer to be accounted for partially as a sale and partially as a secured borrowing?

A—A call that gives the transferor the ability to unilaterally cause whoever holds the transferred financial asset to return the remaining portion of the entire financial asset to the transferor and provides more than a trivial benefit to the transferor precludes sale accounting for the entire financial asset (paragraph 50). Statement 140 requires that derecognition provisions be applied to a transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset. Statement 140 prohibits accounting for a transfer of an entire financial asset or a participating interest in an entire financial asset partially as a sale and partially as a secured borrowing. (See Question 49.) [Added 6/09.]

~~Yes. Statement 140 requires a transferred amortizing, individual financial asset to be bifurcated in the manner described if the transferor is entitled to repurchase part of it, assuming the other provisions of paragraph 9 have been met. Under paragraph 9(c)(2), a call attached to specific transferred assets at a fixed price results in the transferor's maintaining effective control over the transferred assets subject to that call and, therefore, precludes sale accounting. In this case, the specific asset over which the transferor retains control is the remaining principal balance once the asset amortizes to the specified threshold. The transferor has no effective control over the portion of the financial asset that will be collected before then, so the transfer of that portion of the asset should be accounted for as a sale.~~

~~Similarly, if a transferor holds an attached call option to repurchase the individual loans that remain from an entire portfolio of prepayable loans that were transferred in a securitization transaction, once prepayments have reduced the portfolio balance to some specified amount, then sale accounting is precluded only for the transfer of the remaining principal balance subject to the call, not the whole portfolio of loans.~~

~~Also similarly, i~~If a transferor holds a call option to repurchase at any time a few specified, individual loans from an entire ~~portfolio~~ group of loans transferred in a securitization transaction, then sale accounting is precluded only for the specified loans subject to the call, not the whole ~~portfolio~~ group of loans. In contrast, if the transferor holds a call option to repurchase from the ~~portfolio~~ group any loans it chooses, up to some specified limit, then ~~paragraph 86(a) of Statement 140 precludes~~ sale accounting is precluded for the transfer of the entire ~~portfolio~~ group while that option remains outstanding. Refer to Questions 49 and 55. [Revised 6/09.]

51. *Q*—Would a transferor's contractual right to repurchase, at any time, a loan ~~participation~~ that is not a readily obtainable financial asset preclude sale accounting? [Revised 6/09.]

A—Yes, ~~except in the unlikely circumstance that the contractual right is freestanding and does not constrain the transferee. As explained in paragraph 106, a loan participation can only be accounted for as a sale if all of the criteria in paragraph 9 are met. P~~paragraph 9(b) provides that each transferee must have the right to pledge or exchange the assets it received and that no condition both constrains the transferee from taking advantage of its right to pledge or exchange and provides more than a trivial benefit to the transferor. The transferor's contractual right to repurchase a loan ~~participation~~ is effectively a call option, and paragraph 32 notes that a freestanding call option written by a transferee to the transferor may benefit~~s~~ the transferor and, if the transferred financial assets are not readily obtainable in the marketplace, is likely to constrain a transferee. Furthermore, if the transferor's right to repurchase is not freestanding but rather attached to and transferable with the ~~participation~~loan, paragraph 9(c)(2) provides an example that states that ~~precludes sale accounting for transfers in which~~ the transferor maintains effective control over the transferred financial assets through "an agreement that provides the transferor with both the unilateral ability to ~~unilaterally~~ cause the holder to return specific financial assets and a more-than-trivial benefit attributable to that ability, other than through a cleanup call. . . ." Paragraphs 50–54 provide additional implementation guidance on the examples in paragraph 9(c). ~~. . ." Paragraph 50 states that while such an attached call may not constrain a transferee, it could result in the transferor's maintaining effective control over the transferred asset "because the attached call gives the transferor the ability to unilaterally cause whoever holds that specific asset to return it" Refer to Question 49.~~ [Revised 6/09.]

52. [Deleted 6/09.]

~~*Q*—In certain industries, a typical customer's borrowing needs often exceed its bank's legal lending limits. To accommodate the customer, the bank may "participate" the loan to other banks (that is, transfer under a participation agreement a portion of the customer's loan to one or more participating banks). In those situations, a noncontractual *understanding* may exist among the participants. Under that noncontractual understanding, the participating banks will return some portion of the loan at par to the lending bank if its legal lending limit increases. The noncontractual understanding is not an enforceable right, although the participating banks generally comply. Those loans generally are not-readily-obtainable assets, and the participating banks are not constrained from selling their interest in the participation. Does this noncontractual understanding constitute a *unilateral ability to reclaim specific transferred assets?*~~

~~*A*—No. Although the concept (unilateral ability to reclaim specific transferred assets) in paragraph 9(c)(2) of Statement 140 is broader than the concept it replaces (an agreement that entitles the transferor to repurchase transferred assets that are not readily obtainable) in paragraph 9(c)(2) of Statement 125, the lead bank is not in a position to unilaterally reclaim the specific transferred assets. Although the participating bank may choose to comply with the lead bank's request, and may be motivated to do so, for example, by the prospect of future business dealings, it is not contractually obligated to comply. Whether the transferor benefits from knowing where the assets are is not relevant, since the informal understanding does not constrain the transferee from selling or pledging the assets.~~

53. *Q*—Under Statement 140, does a transfer of a debt security classified as held-to-maturity that occurs for a reason other than those specified in paragraphs 8 and 11 of FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* taint the entity's held-to-maturity portfolio?

A—The answer depends on the accounting for the transfer. If the transfer of a held-to-maturity debt security is accounted for as a sale under Statement 140 and it is transferred for a reason other than those specified in paragraphs 8 and 11 of Statement 115, then the transfer would taint the held-to-maturity portfolio. However, if the transfer is accounted for as a secured borrowing, then the transfer would not taint the held-to-maturity portfolio.[14]

Whether a transfer of a debt security is accounted for as a sale under Statement 140 depends on whether the ~~criteria~~ conditions in paragraph 9 are met. In repurchase transactions involving readily obtainable held-to-maturity debt securities, the ~~criteria~~ conditions set forth in paragraphs 47–49, which are an integral part of the standards in paragraph 9, must be carefully evaluated to determine whether the transaction should be accounted for as a sale or secured borrowing. For example, if the security that is required to be returned has a different maturity or has a different contractual interest rate from the transferred security, the substantially-the-same criterion would not be met. In that case, effective control would not be maintained under paragraph 9(c) and the transfer would be accounted for as a sale, assuming the other requirements ~~conditions~~ in paragraph~~s~~ 9~~(a) and 9(b)~~ are met. [Revised 6/09.]

54. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity. Relevant effective control guidance is included in paragraph 52 of Statement 140, as amended by Statement 166.]

~~*Q*—Can a transferor recognize a sale for a transfer of assets a if it holds a call option that is "embedded" in the beneficial interests issued by the qualifying SPE?~~

~~*A*—Not if, under its price and terms, the call conveys more than a trivial benefit to the transferor, as discussed in paragraphs 52 and 53. Paragraph 52 states that "for example, if an embedded call allows a transferor to buy back the beneficial interests of a qualifying SPE at a fixed price, then the transferor remains in effective control of the assets underlying those beneficial interests." Refer to Question 49.~~

55. *Q*—Assuming that all of the other ~~criteria~~ conditions of paragraph 9 are met, is sale accounting appropriate if a "cleanup call" on a ~~pool~~ group of financial assets in ~~a qualifying SPE~~ a securitization entity is held by a party other than the servicer? For example, sometimes the fair value of beneficial interests ~~retained~~ obtained by a transferor of financial assets who is not the servicer or an affiliate of the servicer is adversely affected by the amount of transferred financial assets declining to a "low level." If such a transferor has a call exercisable when transferred financial assets decline to a specified low level, could that be a cleanup call? [Revised 6/09.]

A—No. Paragraph 364 defines a *cleanup call* as follows:

> An option held by the *servicer or its affiliate,* which may be the transferor, to purchase the remaining transferred financial assets, or the remaining beneficial interests not held by the transferor, its affiliates, or its agents in an ~~qualifying SPE~~ entity (or in a series of beneficial interests in transferred financial assets within an ~~qualifying SPE~~entity), if the amount of outstanding financial assets or beneficial interests falls to a level at which the cost of servicing those assets or beneficial interests becomes burdensome in relation to the benefits of servicing. [Emphasis added.] [Revised 6/09.]

Therefore, the transferor's call on the transferred financial assets in the ~~qualifying SPE~~ securitization entity is not a cleanup call for accounting purposes because it is not the servicer or an affiliate of the servicer. [Revised 6/09.]

~~However, the call option only partially precludes sale accounting because the call option can only be exercised when the assets amortize to a pre-specified level.~~

~~As a result, assuming the transfer met the other provisions of paragraph 9, the transferor would record the transfer as a partial sale. Refer to Questions 49 and 50.~~

56. *Q*—In a securitization transaction involving not-readily-obtainable financial assets, may a

[14]Questions 16 and 17 of the FASB Special Report, *A Guide to Implementation of Statement 115 on Accounting for Certain Investments in Debt and Equity Securities,* address whether securities classified as held-to-maturity may be pledged as collateral and subject to a repurchase agreement, respectively.

transferor that is also the servicer hold a cleanup call if it "contracts out the servicing" to a third party (that is, enters into a subservicing arrangement with a third party) without precluding sale accounting? [Revised 6/09.]

A—Yes. Under a subservicing arrangement, the transferor remains the servicer from the perspective of the ~~qualifying SPE~~ securitization entity because the ~~qualifying SPE~~ securitization entity does not have an agreement with the subservicer (that is, the transferor remains liable if the subservicer fails to perform under the subservicing arrangement). However, if the transferor sells the servicing rights to a third party (that is, the agreement for servicing is between the ~~qualifying SPE~~ securitization entity and the third party subsequent to the sale of the servicing rights), then the transferor could not hold a cleanup call. Refer to Question 55. [Revised 6/09.]

Measurement of Assets and Liabilities upon Completion of a Transfer

57. *Q*—Could a transferor's exchange of one form of beneficial interests in financial assets that have been transferred into a trust that is consolidated by the transferor for an equivalent, but different, form of beneficial interests in the same transferred financial assets be accounted for as a sale under Statement 140? [Revised 6/09.]

A—No. Not only would this exchange not be a sale, it might not even be a transfer under Statement 140. If the exchange described is with the trust that initially issued the beneficial interests, then the exchange is not a transfer under Statement 140. Paragraph 364 defines *transfer* as "the conveyance of a noncash financial asset by and to someone other than the issuer of that financial asset." If the exchange is not a transfer, then the provisions of paragraph ~~10~~11 would not be applied to the transaction.

58. [Deleted 6/09 because Statement 140, as amended by Statement 166, requires that derecognition provisions be applied to a transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset. Paragraph 10 of Statement 140, as amended by Statement 166, describes how a transferor accounts for a transfer of a component of a financial asset that represents a participating interest that satisfies the conditions to be accounted for as a sale. Paragraph 11 of Statement 140, as amended by Statement 166, describes how a transferor accounts for a transfer of an entire financial asset or group of entire financial assets that satisfies the conditions to be accounted for as a sale.]

~~*Q*—How should transferred components of financial assets and interests that continue to be held by a transferor be accounted for upon completion of a transfer? [Revised 3/06.]~~

~~*A*—Upon completion of a transfer, the transferor continues to carry in its statement of financial position any interests it continues to hold in the transferred assets, including beneficial interests in assets transferred to a qualifying SPE in a securitization and undivided interests, pursuant to paragraph 10 of Statement 140. Paragraph 10 also requires upon completion of a transfer of financial assets that a transferor initially recognize and measure at fair value, if practicable, servicing assets and servicing liabilities that require recognition under paragraph 13 of Statement 140. It also requires that the transferor allocate the previous carrying amount between the assets sold, if any, and the interests that continue to be held by the transferor, if any, based on their relative fair values at the date of transfer. [Revised 3/06.]~~

~~Paragraph 11 of Statement 140 requires that assets obtained and liabilities incurred in consideration as proceeds of a sale be recognized at fair value unless it is not practicable to do so. Paragraph 56 of Statement 140 states that proceeds from a sale of financial assets consist of the cash and any other assets obtained, including separately recognized servicing assets, in the transfer less any liabilities incurred, including separately recognized servicing liabilities. [Revised 3/06.]~~

~~Interests that continue to be held by a transferor and assets obtained and liabilities incurred upon completion of a transfer of financial assets should be recognized separately. Statement 140 focuses "principally on the initial recognition and measurement of assets and liabilities that result from transfers of financial assets (paragraph 306 of Statement 140). Statement 140 addresses subsequent measurement for servicing assets and servicing liabilities in paragraphs 13A and 13B and 63(d)–63(g). Other~~

~~assets and liabilities recognized upon completion of a transfer should be subsequently measured according to other existing accounting pronouncements and related guidance. For example:~~

- ~~Interest-only strips, interests that continue to be held by a transferor in securitizations, loans, other receivables, or other financial assets that can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment (except for instruments that are within the scope of Statement 133) should be initially recognized according to paragraphs 10 and 11 of Statement 140 and, pursuant to paragraph 14 of Statement 140, subsequently measured like investments in debt securities classified as available-for-sale or trading under Statement 115, as amended by Statement 140.~~
- ~~Equity securities that have readily determinable fair values should be initially recognized according to paragraphs 10 of Statement 140 (if they are interests that continue to be held by a transferor) and 11 of Statement 140 (if they are received as proceeds of the transfer) and subsequently measured in accordance with Statement 115.~~
- ~~Debt securities should be initially recognized according to paragraph 10 of Statement 140 (if they are interests that continue to be held by a transferor) or paragraph 11 of Statement 140 (if they are received as proceeds of the transfer) and subsequently measured in accordance with Statement 115, FASB Statement No. 65, *Accounting for Certain Mortgage Banking Activities,* as amended by FASB Statement No. 134, *Accounting for Mortgage-Backed Securities Retained after the Securitization of Mortgage Loans Held for Sale by a Mortgage Banking Enterprise,* FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments,* and EITF Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests That Continue to Be Held by a Transferor in Securitized Financial Assets," as applicable.~~
- ~~Derivative financial instruments should be initially recognized at fair value (according to paragraph 56 of Statement 140) and subsequently measured in accordance with existing accounting pronouncements and related guidance on derivative instruments including Statement 133. [Revised 3/06; 6/06.]~~

59. [Deleted 6/09 because Statement 140, as amended by Statement 166, states that any beneficial interest obtained in the transfer of an entire financial asset or a group of entire financial assets accounted for as a sale are considered proceeds of the sale and are recognized and initially measured at fair value.]

~~*Q*—How does a transferor account for a beneficial interest in transferred financial assets if it cannot determine whether that beneficial interest is a new asset or an interest that continues to be held by a transferor? [Revised 3/06.]~~

~~*A*—Paragraph 58 states that "if a transferor cannot determine whether an asset is an interest that continues to be held by a transferor or proceeds from the sale, the asset shall be treated as proceeds from the sale. . . ." Paragraph 56 states that "all proceeds and reductions of proceeds from a sale shall be initially measured at fair value, if practicable." [Revised 3/06.]~~

60. [Deleted 6/09 because Statement 140, as amended by Statement 166, states that any beneficial interest obtained in the transfer of an entire financial asset or a group of entire financial assets accounted for as a sale are considered proceeds of the sale and are recognized and initially measured at fair value.]

~~*Q*—In certain securitization transactions, more than one transferor contributes assets to a single qualifying SPE. Those transactions are sometimes referred to as *securitization transactions that "commingle" assets*. For example, Transferor A transfers a Treasury bond and Transferor B transfers a zero-coupon corporate bond to the same qualifying SPE. At the date of the transfers, the fair value of the Treasury bond and the zero-coupon corporate bond are equal. In exchange, each transferor receives a 40 percent beneficial interest in the qualifying SPE entitling each participant to a 40 percent interest in each cash flow (that is, each beneficial interest holder receives the same tranche of the trust certificates and is entitled to 40 cents of~~

~~each dollar collected). Investor C (who is not an affiliate or agent of either transferor) invests cash in return for the last beneficial interest (which gives it the right to receive 20 cents of each dollar collected). The cash invested by Investor C is distributed pro rata to Transferors A and B at the transfer date. [Revised 4/02.]~~

~~What is the basis for determining whether a beneficial interest in transferred financial assets is a new asset or an interest that continues to be held by a transferor in a securitization structure that commingles assets? [Revised 3/06.]~~

~~*A*—A transferor should treat the beneficial interests as new assets to the extent that the sources of the cash flows to be received by the transferor are assets transferred by another entity. Any beneficial interests whose cash flows are derived from assets transferred by the transferor should be treated as interests that continue to be held by the transferor. Any derivatives, guarantees, or other contracts entered into by the qualifying SPE to "transform" the transferred assets are considered to be new assets, not commingled assets, because they were entered into by the qualifying SPE rather than transferred into the qualifying SPE by another entity. [Revised 3/06.]~~

~~In the example provided, Transferor A would treat 50 percent of its beneficial interests as interests that continue to be held by the transferor and 50 percent of its beneficial interests as new assets (proceeds from the transfer). Transferor A would also treat the cash received at the transfer date as proceeds. [Revised 4/02; 3/06.]~~

~~The Board acknowledges that determining whether a beneficial interest in a securitization is a new asset or an interest that continues to be held by a transferor may be difficult. Paragraph 272 explains:~~

> ~~The Board believes that it is impractical to provide detailed guidance that would cover all possibilities. A careful examination of cash flows, risks, and other provisions should provide a basis for resolving most questions. However, the Board agreed that it would be helpful to provide guidance if an entity cannot determine how to classify an instrument and decided that in that case the instrument should be considered to be a new asset and thus part of the proceeds of the sale initially measured at fair value.~~

~~[Revised 3/06.]~~

~~As part of its response to those issues, the Board decided to include in paragraph 58 the default provision that "if a transferor cannot determine whether an asset is an interest that continues to be held by a transferor or proceeds from the sale, the asset shall be treated as proceeds from the sale. . . ." In the case of commingled transfers from different transferors, each transferor to a qualifying SPE is eligible to apply the consolidation guidance in paragraph 46 of Statement 140. Refer to Question 36. [Revised 3/06.]~~

61. *Q*—An entity transfers debt securities to an ~~qualifying SPE~~ unconsolidated entity that has a predetermined life in exchange for (a) cash and (b) the right to receive proceeds from the eventual sale of the securities. For example, a third party holds a beneficial interest that is initially worth 25 percent of the fair value of the assets of the ~~qualifying SPE~~ entity at the date of transfer. The ~~qualifying SPE~~ entity is required to sell the transferred securities at a predetermined date and liquidate the ~~qualifying SPE~~ entity at that time. Assume the facts in that example and the following additional facts:

- The beneficial interests are issued in the form of debt securities.
- Prior to the transfer, the debt securities were accounted for as available-for-sale securities in accordance with Statement 115.

[Revised 6/09.]

Does the transferor have the option to classify the debt securities as trading at the time of the transfer?

A—It depends on whether the transfer is accounted for as a sale or as a secured borrowing. If a transfer of a group of entire financial assets satisfies the conditions to be accounted for as a sale, paragraph 11 of Statement 140, as amended by Statement 166, requires that any assets obtained or liabilities incurred in the transfer be recognized and initially measured at fair value. If the transfer in the example is accounted for as a sale, the transferor would account for the debt securities received as new assets and would have the option to classify the debt securities received as trading securities. If the transfer is accounted for as a secured borrowing, paragraph 12 of Statement 140, as amended by Statement 166, requires the transferor to continue to report the transferred debt securities in its statement of financial position with no change in their measurement (that is, basis of accounting). The guidance on transfers in paragraph 15 of Statement 115, which ~~Generally, no. That response is based on the following:~~

- ~~The Statement 115 securities held by the transferor after the transfer convey rights to the same cash flows as did the Statement 115 securities held before the transfer.~~
- ~~Paragraph 15 of Statement 115~~ explains that transfers into or from the trading category should be rare, would continue to apply. [Revised 6/09.]

~~In contrast, i~~If the transferred financial assets were not Statement 115 securities prior to the transfer that was accounted for as a sale but the beneficial interests were issued in the form of debt securities or in the form of equity securities that have readily determinable fair values, then the transferor would have the opportunity to decide the appropriate classification of the ~~transferred assets at the date of the transfer~~beneficial interests received as proceeds from the sale. [Revised 6/09.]

62. *Q*—In certain transfers that are accounted for as sales, the transferor obtains ~~retains~~ an interest that should be subsequently accounted for under EITF Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Transferor's Beneficial Interests in Securitized Financial Assets Obtained in a Transfer Accounted for as a Sale." If the transferred financial asset was accounted for as available for sale under Statement 115 prior to the transfer, how should the transferor account for amounts in other comprehensive income at the date of transfer? [Revised 6/09.]

A—Paragraph 11 of Statement 140, as amended by Statement 166, requires a transferor to derecognize a transferred financial asset upon completion of a transfer of an entire financial asset that satisfies the conditions to be accounted for as a sale. As a result, the amount in other comprehensive income will be recognized in earnings at the date of transfer.~~The application of Issue 99-20 should not result in recognition in earnings of an unrealized gain or loss that had been recognized in accumulated other comprehensive income before it is realized. The following example illustrates that concept.~~ [Revised 6/09.]

~~An entity transfers financial assets that are appreciated debt securities to a qualifying SPE in exchange for 80 percent of the beneficial interests in the qualifying SPE and $30 in cash. The original cost basis for the debt securities is $100, and their fair value is $150 at the date of transfer to the qualifying SPE. Because those securities are accounted for as available-for-sale securities under Statement 115, the carrying amount at the date of transfer is $150 and the unrealized gain in other comprehensive income is $50. The qualifying SPE also issues, for $30, beneficial interests entitling the unrelated investor to a fixed rate of interest for 5 years. On the fifth anniversary of the qualifying SPE, the assets remaining in it will be sold and the beneficial interest holders (the investor and the transferor) will receive the proceeds.~~

~~For purposes of applying Issue 99-20, the initial investment in the retained beneficial interests is the allocated carrying amount, that is, $120. Twenty percent or $10 of the unrealized gain of $50 would be recognized at the time of transfer. The remaining unrealized gain of $40 should remain in accumulated other comprehensive income until the qualifying SPE sells the assets remaining in the qualifying SPE. The amount of the unrealized gain in other comprehensive income ignores the effect of income taxes.~~

63. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity and Question 62 provides the relevant guidance.]

~~*Q*—Assume the same facts as in Question 62, except that the qualifying SPE is directed (at inception) to sell the transferred debt securities at a predetermined date and then to reinvest the proceeds in different debt instruments that mature at the same date that the qualifying SPE~~

~~liquidates. When should the transferor recognize the unrealized gain of $40 that remained in accumulated other comprehensive income at the date of transfer?~~

~~*A*—The transferor should recognize a sale, and a gain or loss, when the transferred assets are sold by the qualifying SPE. At that point, the transferor's interest is no longer a beneficial interest in the transferred assets but rather a beneficial interest in the different debt instruments. In the example provided above, the $40 unrealized gain in accumulated other comprehensive income should be recognized in the transferor's net income when the qualifying SPE sells the transferred assets.~~

64. *Q*—Assume an entity transfers a bond to an ~~qualifying SPE~~ unconsolidated entity for cash and beneficial interests. When the transferor purchased the bond, it paid a premium for it (or bought it at a discount), and that premium (or discount) was not fully amortized (or accreted) at the date of the transfer. In other words, the carrying amount of the bond included a premium (or discount) at the date of the transfer. Would that previously existing premium (or discount) continue to be amortized (or accreted)? [Revised 6/09.]

A—~~Yes,~~ It depends on whether the transfer is accounted for as a sale or as a secured borrowing. If the transfer of the bond is accounted for as a secured borrowing, paragraph 12 of Statement 140, as amended by Statement 166, requires a transferor to continue to report the transferred financial asset in its statement of financial position with no change in measurement. As a result, the transferor would continue to amortize (or accrete) the premium (or discount). [Revised 6/09.]

Paragraph 11 of Statement 140, as amended by Statement 166, requires a transferor to derecognize an entire financial asset or a group of entire financial assets upon completion of a transfer that satisfies the conditions to be accounted for as a sale. Any beneficial interests received as proceeds would be initially recognized at fair value. As a result, the previously existing premium (or discount) would not continue to be amortized (or accreted); rather, the unamortized (or nonaccreted) amount would be included in the calculation of the gain (or loss) as of the transfer date.~~but only to the extent a sale has not occurred because the transferor continues to hold beneficial interests in the bond. Paragraph 10 of Statement 140 requires that, upon completion of any transfer, a transferor (a) continue to carry in its statement of financial position any interest it continues to hold in the transferred assets and (b) allocate the previous carrying amount between the assets sold, if any, and the interests that continue to be held by the transferor, if any, based on their relative fair values at the date of transfer. That allocation process may change the amount of the premium (or discount) that is amortized (or accreted) thereafter as an adjustment of yield pursuant to FASB Statement No. 91, *Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases*. Issue 99-20 may also apply in certain circumstances.~~ [Revised 3/06; 6/09.]

65. [Deleted 6/09 because Statement 140, as amended by Statement 166, requires that derecognition provisions be applied to a transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset.

~~*Q*—In a transfer of financial assets in which the transferor continues to hold beneficial interests in 80 percent of the transferred assets, should the remaining 20 percent of transferred assets be treated as sold, assuming that all the criteria in paragraph 9 of Statement 140 have been met? [Revised 3/06.]~~

~~*A*—Yes. Paragraph 9 of Statement 140 specifies that "a transfer of financial assets (or all or a portion of a financial asset) in which the transferor surrenders control over those financial assets shall be accounted for as a sale *to the extent* that consideration other than beneficial interests in the transferred assets is received in exchange" (emphasis added). [Revised 3/06.]~~

66. [Deleted 6/09 because FASB Statement No. 157, *Fair Value Measurements,* defines fair value and establishes a framework for measuring fair value.]

~~*Q*—Does the fair value measurement of an interest that continues to be held by the transferor in a securitization that is classified as either~~

~~available-for-sale or trading under Statement 115 include the estimated cash flows associated with those interests that are generated from receivables that do not yet exist but that will be originated and transferred during the revolving period (such as in securitizations with *revolving features* or *prefunding provisions*)? [Revised 3/06.]~~

~~*A*—No. Paragraph 78 of Statement 140 explains that "gain or loss recognition for revolving-period receivables sold to a securitization trust is limited to receivables that exist and have been sold." [Revised 3/06.]~~

67. *Q*—Can the method used by the transferor for providing "recourse" affect the accounting for ~~the~~a transfer to an unconsolidated entity? [Revised 6/09.]

A—Yes. If the transfer does not consist of an entire financial asset or a group of entire financial assets, the transferred financial asset must meet the definition of a participating interest (as discussed in paragraph 8B of Statement 140, as added by Statement 166). Paragraph 8B(c) of Statement 140, as added by Statement 166, prohibits participating interest holders from having recourse to the transferor (or its consolidated affiliates included in the financial statements being presented or its agents) or to each other, other than standard representations and warranties, ongoing contractual obligations to service the entire financial asset and administer the transfer contract, and contractual obligations to share in any set-off benefits received by any participating interest holder. That recourse would result in the transfer being accounted for as a secured borrowing. [Revised 6/09.]

If the transfer consists of an entire financial asset or a group of entire financial assets, the following guidance would apply: [Revised 6/09.]

~~However, before~~Before the method of recourse can be evaluated for the appropriate accounting treatment, the entity must first determine whether a sale has occurred because in some jurisdictions recourse might mean that the transferred financial assets have not been isolated beyond the reach of the transferor, any of its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented, and its creditors. [Revised 6/09.]

A transferor may ~~continue to~~ hold ~~all or~~ some portion of the credit risk associated with ~~transferred~~ a transfer of an entire financial asset or a group of entire financial assets. For example, a transferor may incur a liability to reimburse the transferee, up to a certain limit, for a failure of debtors to pay when due (a recourse liability). In that case, a liability should be separately recognized and initially measured at fair value. That liability should be subsequently measured according to accounting pronouncements for measuring similar liabilities. In other cases, a transferor may provide credit enhancement ~~by continuing to hold a~~ through its ownership of a beneficial interest in the transferred financial assets if that beneficial interest ~~that~~ is not paid until the ~~to the transferor after~~ other investors in the transferred financial assets are paid, thereby resulting in the transferor absorbing much of the related credit risk. ~~If there is no liability beyond those subordinated interests, then the~~ As a result, the beneficial interests that ~~continue to be held~~ are obtained by the transferor should be initially recognized according to paragraph ~~10~~11 of Statement 140. ~~and should be subsequently measured like other interests that continue to be held by the transferor in the same form. Therefore, no recourse liability would be needed.~~ [Revised 3/06; 6/09.]

68. *Q*—What should the transferor consider when determining whether ~~retained~~ credit risk is a separate liability or part of a beneficial interest that ~~continues to be held~~ has been obtained by the transferor? [Revised 3/06; 6/09.]

A—The transferor should focus on the source of cash flows in the event of a claim by the transferee. If the transferee can only "look to" cash flows from the underlying financial assets, the transferor has ~~retained~~ obtained a portion of the credit risk only through the interest it ~~continues to hold~~ obtained and a separate obligation should not be recognized. Credit losses from the underlying assets would affect the measurement of the interest that the transferor obtained~~continues to hold~~. In contrast, if the transferor could be obligated for more than the cash flows provided by the interest it ~~continues to hold~~ obtained and, therefore, could be required to "write a check" to reimburse the transferee for credit-related losses on the underlying assets, the transferor would record a separate liability~~ rather than an asset valuation allowance on the date of the transfer~~. [Revised 3/06; 6/09.]

69. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the fair value practicability exception.]

~~*Q*—What is meant by the term *practicable* as used in paragraphs 11(e) and 71?~~

~~*A*—The Board did not define the term *practicable* in Statement 140. However, the Board explained its reasoning for the practicability exception. Paragraph 298 states:~~

> ~~There was concern that, in some cases, the best estimate of fair value would not be sufficiently reliable to justify recognition in earnings of a gain following a sale of financial assets with continuing involvement, because errors in the estimate of asset value or liability value might result in recording a nonexistent gain.~~

~~The Board was asked to clarify the meaning of the term *practicable,* especially in relation to the use of the same term in Statement 107. The Board ultimately decided not to provide additional guidance about applying that term. Therefore, determining when it is not practicable to estimate the fair value of assets or liabilities requires judgment. In those circumstances, paragraph 71 establishes special requirements if it is not practicable to estimate the fair value of assets obtained or liabilities incurred. Paragraph 17(d) also requires that an entity provide a description of the items for which it was not practicable to estimate the fair value *and the reasons why it was not practicable*. However, in a vast majority of circumstances, it should be practicable to estimate fair values.~~

70. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the fair value practicability exception.]

~~*Q*—At what amount should the transferor initially recognize an asset obtained or a liability incurred for which, at the date of transfer, it was not practicable to estimate the fair value?~~

~~*A*—Paragraph 71 states:~~

> ~~If it is not practicable to estimate the fair values of assets [at the time of transfer], the transferor shall record those assets at zero [emphasis added]. If it is not practicable to estimate the fair values of liabilities, the transferor shall recognize no gain on the transaction and shall record those liabilities at the greater of:~~
>
> ~~a. The excess, if any, of (1) the fair values of assets obtained less the fair values of other liabilities incurred, over (2) the sum of the carrying values of the assets transferred~~
>
> ~~b. The amount that would be recognized in accordance with FASB Statement No. 5, *Accounting for Contingencies,* as interpreted by FASB Interpretation No. 14, *Reasonable Estimation of the Amount of a Loss.*~~

~~That is, Statement 140 requires that assets be recorded at fair value or at zero if it is not practicable to estimate the fair value of assets at the date of the transfer, not at some amount that is not an estimate of fair value.~~

~~Paragraph 299 notes that the practicability exception does not extend to the transferee, since as ". . . the purchaser of the assets, [the transferee] should be able to value all assets and any liabilities it purchased or incurred, presumptively based on the purchase price paid."~~

71. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the fair value practicability exception.]

~~*Q*—Paragraph 71 of Statement 140 provides guidance on accounting for assets and liabilities in cases in which, at the date of transfer, it is not practicable to estimate their fair values. However, if at a later date the transferor can estimate the fair value of an asset or liability for which it was not practicable at the date of the transfer (that is, it becomes practicable), should that asset or liability be remeasured? [Revised 3/06.]~~

~~*A*—If it becomes practicable for the transferor to estimate the fair value of the affected asset at a later date, the transferor would not remeasure the asset or the resulting gain or loss under Statement 140. Paragraph 13A of Statement 140 requires that if it is not practicable to~~

~~initially measure a servicing asset or servicing liability at fair value, the transferor shall initially recognize the servicing asset or servicing liability in accordance with paragraph 71 of Statement 140 and shall include it in a class of servicing assets and servicing liabilities that is subsequently measured using the amortization method. Paragraphs 63(f) and 63(g) of Statement 140 require servicing assets and servicing liabilities subsequently measured using the amortization method to be evaluated for impairment or increased obligation. In other cases, the transferor may be required to subsequently adjust that asset's carrying amount depending on the accounting pronouncement that addresses its subsequent measurement. One possible result is that an asset may be initially recognized at zero or a liability may be initially recognized at something other than fair value because of the practicability exception in Statement 140 and then subsequently measured at an estimate of fair value with changes in fair value recognized according to the requirements of the relevant pronouncement. For example, some assets may be required to be subsequently measured at fair value even if it is not practicable to estimate their fair value at the date of transfer (for example, Statement 115 does not provide a practicability exception). If it becomes practicable for the transferor to estimate the fair value of an affected liability at a later date, the transferor would remeasure that liability under Statement 140 only if it is a servicing liability. [Revised 3/06.]~~

~~The transferor would remeasure a servicing liability but not below the amortized measurement of its initially recognized amount. Paragraph 13A requires an entity that has elected to subsequently measure a class of separately recognized servicing assets and servicing liabilities using the amortization method to amortize servicing liabilities in proportion to and over the period of estimated net servicing loss, and assess servicing liabilities for increased obligation based on fair value at each reporting date. Paragraph 63(g) of Statement 140 requires:~~

> ~~For servicing liabilities subsequently measured using the amortization method, if subsequent events have increased the fair value of the liability above the carrying amount, . . . the servicer shall revise its earlier estimates and recognize the increased obligation as a loss in earnings. . . .~~

~~[Revised 3/06.]~~

~~For other liabilities, other accounting pronouncements that address subsequent measurement may require that the transferor subsequently adjust an affected liability's carrying amount.~~

72. *Q*—Must a transferor recognize in earnings the gain or loss that results from a transfer of financial assets that is accounted for as a sale, or may the transferor elect to defer recognizing the resulting gain or loss in certain circumstances?

A—Paragraphs 10(d) and 11(d) require~~s~~ that upon the completion of a transfer of financial assets that satisfies the conditions to be accounted for as a sale, any resulting gain or loss must be recognized in earnings. *It is not appropriate for the transferor to defer any portion of a resulting gain or loss* (or to eliminate "gain on sale" accounting, as it is sometimes described in practice).~~As described previously in Question 70, paragraph 71 provides special requirements if it is not practicable to estimate the fair value of assets obtained or liabilities incurred.~~ [Revised 6/09.]

73. *Q*—Does Statement 140 require disclosures about the assumptions used to estimate fair values of the transferor's interests~~that continue to be held by a transferor~~ in securitized financial assets or of other assets obtained and liabilities incurred~~as proceeds~~ in a transfer? [Revised 3/06; 6/09.]

A—Yes. See paragraph 17(f) of Statement 140, as amended by Statement 166.~~Paragraph 17(h)(3) of Statement 140 requires the disclosure of "the key assumptions used in measuring the fair value of interests that continue to be held by the transferor and servicing assets and servicing liabilities, if any, at the time of securitization . . ." (footnote omitted). Paragraph 17(i)(2) of Statement 140 requires disclosure of "the key assumptions used in subsequently measuring the fair value of those interests . . ." held at the most recent balance sheet date. Finally, paragraph 17(i)(3) of Statement 140 requires a sensitivity analysis or stress test showing the hypothetical ef-~~

~~fect of changes in those assumptions on the fair value of those interests (including any servicing assets or servicing liabilities).~~ [Revised 3/06; 6/09.]

~~Paragraph 17(d) of Statement 140 requires that "if it is not practicable to estimate the fair value of certain assets obtained or liabilities incurred in transfers of financial assets during the period," an entity shall disclose "a description of those items and the reasons why it is not practicable to estimate their fair value." [Revised 3/06.]~~

74. [Deleted 6/09 because Statement 140, as amended by Statement 166, requires that all assets obtained and liabilities incurred by the transferor in a transfer accounted for as a sale be considered proceeds from the sale and measured at fair value.]

~~*Q*—A transferor transfers loans with a fair value of $100 to a qualifying SPE in exchange for cash of $100. However, to enhance the credit rating of the beneficial interests in the qualifying SPE, a *cash reserve* account is created in connection with the transfer. That cash reserve account is funded with $20 of the transferor's proceeds and $20 of additional cash contributed by the transferor. The cash will be returned to the transferor at some date in the future provided that a certain level of collections occurs but will be reduced to the extent that collections fall short of that level.~~

~~Are proceeds (in a transfer that is accounted for as a sale) that are placed in a cash reserve account (as a form of a credit enhancement) a new asset or an interest that continues to be held by the transferor in transferred assets? [Revised 3/06.]~~

~~*A*—The proceeds that are placed in a cash reserve account are an interest that continues to be held by the transferor. Paragraph 58 of Statement 140 specifies that a *cash reserve* account is an interest that continues to be held by the transferor. That answer also would apply if the seller collects the proceeds and then deposits a portion of those proceeds in the cash reserve account. Refer to Questions 75–77. [Revised 3/06.]~~

75. *Q*—How should a transferor initially and subsequently measure ~~the interest it continues to hold in~~ credit enhancements (for example, cash reserve accounts) provided in a transfer of an entire financial asset or a group of entire financial assets to an unconsolidated entity that is accounted for as a sale if the balance that is not needed to make up for credit losses is ultimately to be paid to the transferor? [Revised 3/06; 6/09.]

A—Paragraph 11 of Statement 140, as amended by Statement 166, requires all assets obtained and liabilities incurred by the transferor in a transfer of an entire financial asset or a group of entire financial assets that satisfies the conditions to be accounted for as a sale to be recognized and initially measured at fair value. ~~Some credit enhancements (for example, cash reserve accounts and subordinated beneficial interests) should be measured at the date of the transfer by allocating the previous carrying amount between the interests that the transferor continues to hold in the transferred assets and the assets sold, based on their relative fair values. Other credit enhancements (for example, financial guarantees and credit derivatives) are liabilities that are initially measured at their fair values. Question 68 discusses how to determine whether a credit enhancement is a new asset or an interest that continues to be held by the transferor. Questions 76 and 77 discuss techniques for estimating the fair value of an interest that continues to be held by the transferor.~~ [Revised 3/06; 6/09.]

Statement 140 does not specifically address the subsequent measurement of credit enhancements. How much cash the transferor will receive from, for example, a cash reserve account and when it will receive cash inflows depend on the performance of the transferred financial assets. Entities should regularly review those assets for impairment because of their nature.

Entities must look to other guidance for subsequent measurement including impairment~~[15]~~ based on the nature of the credit enhancement. (See Question 122.) [Revised 6/09.]

76. [Deleted 6/09 because Statement 157 defines fair value and establishes a framework for measuring fair value.]

~~*Q*—In certain securitization transactions, the transferor must provide a credit enhancement such as a cash reserve account or a subordinated beneficial interest. As discussed briefly in Question 74, a cash reserve account might work as follows. The transferor retains the majority of the credit risk associated with the transferred assets (for example, loans) by retaining a subordinated tranche (the Z tranche) of the beneficial interests. The transferor also may make a funding deposit into a cash reserve account. As loans are collected by the qualifying SPE, a specified portion of the cash flows attributable to the Z tranche are accumulated in the cash reserve account for possible distribution to the other beneficial interest holders if specified collection targets are not met. However, if those collection targets are met, distributions are to be made from the cash reserve account to the transferor as holder of the Z tranche beneficial interests. How should an entity estimate the fair value of a credit enhancement such as a cash reserve account or subordinated beneficial interest provided by the transferor in a transfer (for purposes of allocating the carrying amount based on relative fair value)?~~

~~*A*—Paragraphs 68–70 provide guidance on how to estimate fair value under Statement 140. Transferors are required to estimate fair value in a manner consistent with that guidance. When estimating the fair value of a credit enhancement, the transferor's assumptions should include the period of time that its use of the asset is restricted, reinvestment income, and potential losses due to uncertainties. Those assumptions must be considered to satisfy the requirement in paragraph 69 to "incorporate assumptions that market participants would use in their estimates of values, future revenues, and future expenses, including assumptions about interest rates, default, prepayment, and volatility" (footnote omitted).~~

~~One valuation technique that might be acceptable is the "cash-out" method. Under the cash-out method, cash flows are discounted from the date the credit enhancement asset becomes available to the transferor (that is, when the cash in the credit enhancement account is expected to be paid out to the transferor, hence the term, *cash out*). Therefore, using an expected present value technique with a risk-free rate or a "best estimate" technique with an appropriate discount rate, the cash-out method estimates the fair value in a manner consistent with paragraph 69 (that is, both the entire period of time that the transferor's use of the asset is restricted and the potential losses due to uncertainties are considered when estimating the fair value of the credit enhancement).~~

~~In contrast, under most "cash-in" methods, the assumed discount period generally ends when the qualifying SPE is expected to collect the specified amount of loans (that is, when the cash is expected to come into the qualifying SPE, hence the term, *cash in*). In some cases, once the cash is "in the qualifying SPE," credit uncertainties arising subsequent to that date that are associated with the transferred assets are not always considered in the estimate of the fair value of the credit enhancement. As a result, the amount calculated under the cash-in method usually is closer to par value or face value than fair value. A method that (a) does not appropriately discount the credit enhancement asset for the entire period it is restricted under the credit enhancement agreement or (b) may not consider all of the credit uncertainties that the market would consider *is not an appropriate method to estimate the fair value of credit enhancements* such as cash reserve accounts and subordinated beneficial interests even though it might be possible for that estimated amount to approximate fair value in certain circumstances. Thus a cash-in method is not appropriate.~~

~~[15]Determining the appropriate literature for evaluating impairment is a matter of facts and circumstances. Other literature that might provide the appropriate guidance includes Statement 5, FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan,* Statement 115, Statement 133, and Issue 99-20.~~

77. [Deleted 6/09 because Statement 157 defines fair value and establishes a framework for measuring fair value.]

~~*Q*—Paragraphs 69 and 70 of Statement 140 indicate that the Board believes that an expected present value technique is superior to traditional "best estimate" techniques in measuring the fair value of interests that continue to be held by the transferor in securitized assets. How might the expected present value technique be applied to such measurements? [Revised 3/06.]~~

~~*A*—Expected present value techniques are discussed and illustrated in general terms in FASB Concepts Statement No. 7, *Using Cash Flow Information and Present Value in Accounting Measurements*. Those techniques consider the likelihood of possible outcomes directly, rather than indirectly through the use of a risk-adjusted discount rate. The following illustration indicates one way in which those techniques might be applied in measuring the fair value, using a cash-out method, of an interest that continues to be held by the transferor in a securitization that was subordinated to investors' interests through a "credit enhancement account," a type of cash reserve account. [Revised 3/06.]~~

~~Illustration—Value of interest that continues to be held by the transferor in securitization of $1,000.00 of $15 year prepayable mortgages, in the form of a credit enhancement account that protects senior beneficial interests [Revised 3/06.]~~

~~Present values of future inflows to transferor under indicated scenario~~

	~~Year~~	~~Very Bad~~	~~Unfavorable~~	~~Most Likely~~	~~Favorable~~	~~Total~~
	~~1~~	~~0~~	~~0~~	~~0~~	~~0~~	
	~~2~~	~~0~~	~~0~~	~~2~~	~~16~~	
	~~3~~	~~0~~	~~1~~	~~24~~	~~31~~	
	~~4~~	~~0~~	~~13~~	~~20~~	~~25~~	
	~~5~~	~~0~~	~~7~~	~~15~~	~~18~~	
	~~6~~	~~0~~	~~9~~	~~14~~	~~15~~	
	~~7~~	~~0~~	~~8~~	~~12~~	~~12~~	
	~~8~~	~~0~~	~~7~~	~~10~~	~~9~~	
	~~9~~	~~0~~	~~6~~	~~8~~	~~7~~	
	~~10~~	~~0~~	~~5~~	~~7~~	~~6~~	
	~~11~~	~~0~~	~~4~~	~~5~~	~~5~~	
	~~12~~	~~1~~	~~3~~	~~4~~	~~4~~	
	~~13~~	~~1~~	~~3~~	~~4~~	~~3~~	
	~~14~~	~~1~~	~~2~~	~~3~~	~~2~~	
	~~15~~	~~6~~	~~12~~	~~11~~	~~6~~	
~~Total~~		~~9~~	~~79~~	~~138~~	~~159~~	
~~Probability~~		~~10%~~	~~20%~~	~~50%~~	~~20%~~	~~100%~~
~~Probability-weighted totals~~		~~$ 0.9~~	~~$ 15.8~~	~~$ 69.2~~	~~$ 31.7~~	~~$117.7~~
		~~**Total expected present value:**~~				~~**$ 118**~~

~~**Notes:** Values derive from supporting scenario worksheets, one of which is shown on the following pages. Working models of those scenario worksheets are available on the FASB website.~~

~~Expected Cash Flow Illustration—Very Bad Scenario~~

~~Year~~	~~Beginning Principal~~	~~Prepays~~	~~Interest~~	~~Total Cash In~~	~~Chargeoffs~~	~~Investors' Share of: Interest~~	~~Investors' Share of: Prepays~~	~~Investors' Share of: Chargeoffs~~
~~1~~	~~1,000~~	~~0~~	~~98~~	~~98~~	~~35~~	~~71~~	~~0~~	~~32~~
~~2~~	~~965~~	~~97~~	~~90~~	~~186~~	~~34~~	~~65~~	~~87~~	~~30~~
~~3~~	~~835~~	~~83~~	~~78~~	~~161~~	~~29~~	~~56~~	~~75~~	~~26~~
~~4~~	~~722~~	~~72~~	~~67~~	~~140~~	~~25~~	~~48~~	~~65~~	~~23~~
~~5~~	~~625~~	~~62~~	~~58~~	~~120~~	~~33~~	~~42~~	~~56~~	~~30~~
~~6~~	~~529~~	~~53~~	~~49~~	~~102~~	~~19~~	~~36~~	~~48~~	~~17~~
~~7~~	~~458~~	~~46~~	~~43~~	~~88~~	~~16~~	~~31~~	~~41~~	~~14~~
~~8~~	~~396~~	~~40~~	~~37~~	~~77~~	~~14~~	~~27~~	~~36~~	~~12~~
~~9~~	~~343~~	~~34~~	~~32~~	~~66~~	~~12~~	~~23~~	~~31~~	~~11~~
~~10~~	~~296~~	~~30~~	~~28~~	~~57~~	~~10~~	~~20~~	~~27~~	~~9~~
~~11~~	~~256~~	~~26~~	~~24~~	~~50~~	~~9~~	~~17~~	~~23~~	~~8~~
~~12~~	~~222~~	~~22~~	~~21~~	~~43~~	~~8~~	~~15~~	~~20~~	~~7~~
~~13~~	~~192~~	~~19~~	~~18~~	~~37~~	~~7~~	~~13~~	~~17~~	~~6~~
~~14~~	~~166~~	~~17~~	~~15~~	~~32~~	~~6~~	~~11~~	~~15~~	~~5~~
~~15~~	~~144~~	~~138~~	~~7~~	~~146~~	~~5~~	~~5~~	~~125~~	~~5~~
~~Totals~~		~~747~~			~~261~~			

~~Explanation~~:

~~In this securitization, credit enhancement is provided to investors in senior beneficial interests using a credit enhancement account (CEA), sometimes called a "cash collateral account."~~

~~Investors are entitled to cash payment of interest, their share of prepayments, and reimbursement for chargeoffs of uncollectable loans, to the extent that cash is available from either the cash inflows from borrowers or the balance of the credit enhancement account.~~

~~Shortfalls in the CEA reimbursement are made up from future available cash inflows.~~

~~Remaining cash inflows are deposited in the credit enhancement account, until its balance exceeds the agreed targeted percentage of the remaining outstanding principal balance. Amounts in excess of the targeted balance may be withdrawn by the transferor.~~

~~The amounts that will be withdrawn by the transferor are its cash inflows from its interest that is continues to hold in the transferred assets. [Revised 3/06.]~~

~~Simplifications for purposes of Illustration:~~

~~Here, the chargeoff and prepayment rates are assumed to be uniform over the life of the securitization, except for a larger chargeoff in year five. Under realistic assumptions, they would vary.~~

~~The loans are non-amortizing, prepayable 15 year loans. Amortizing loans are more common in the United States.~~

~~While prepayments and chargeoffs are assumed to occur evenly throughout the year, CEA calculations are made only at the end of the year.~~

~~Only four scenarios are modeled (one of which is illustrated here). Realistic valuations would include more scenarios.~~

~~Expected Cash Flow Illustration—Very Bad Scenario (continued)~~

~~Due to Investors~~	~~CEA (Shortfall)~~	~~CF out to Investors~~	~~To/(From) CEA~~	~~CEA Balance (Deficit)~~	~~CEA Target~~	~~CF Out to T'or~~	~~Yield Curve~~	~~PV of CF to T'or~~
~~102~~	~~(4)~~	~~98~~	~~0~~	~~(4)~~	~~48~~	~~0~~	~~6.0%~~	~~0~~
~~182~~	~~4~~	~~186~~	~~0~~	~~0~~	~~42~~	~~0~~	~~6.1%~~	~~0~~
~~157~~	~~0~~	~~157~~	~~4~~	~~4~~	~~36~~	~~0~~	~~6.2%~~	~~0~~
~~136~~	~~0~~	~~136~~	~~3~~	~~8~~	~~31~~	~~0~~	~~6.3%~~	~~0~~
~~127~~	~~0~~	~~127~~	~~(7)~~	~~1~~	~~26~~	~~0~~	~~6.4%~~	~~0~~
~~100~~	~~0~~	~~100~~	~~2~~	~~3~~	~~23~~	~~0~~	~~6.5%~~	~~0~~
~~86~~	~~0~~	~~86~~	~~2~~	~~5~~	~~20~~	~~0~~	~~6.6%~~	~~0~~
~~75~~	~~0~~	~~75~~	~~2~~	~~7~~	~~17~~	~~0~~	~~6.7%~~	~~0~~
~~65~~	~~0~~	~~65~~	~~2~~	~~8~~	~~15~~	~~0~~	~~6.8%~~	~~0~~
~~56~~	~~0~~	~~56~~	~~1~~	~~10~~	~~13~~	~~0~~	~~6.9%~~	~~0~~
~~48~~	~~0~~	~~48~~	~~1~~	~~11~~	~~11~~	~~0~~	~~7.0%~~	~~0~~
~~42~~	~~0~~	~~42~~	~~1~~	~~12~~	~~10~~	~~2~~	~~7.1%~~	~~1~~
~~36~~	~~0~~	~~36~~	~~1~~	~~10~~	~~8~~	~~2~~	~~7.2%~~	~~1~~
~~31~~	~~0~~	~~31~~	~~1~~	~~9~~	~~7~~	~~2~~	~~7.3%~~	~~1~~
~~134~~	~~0~~	~~134~~	~~11~~	~~19~~	~~0~~	~~19~~	~~7.4%~~	~~6~~
		~~1,379~~						~~9~~

~~Contract terms and valuation assumptions:~~	**~~Very Bad Scenario~~**
~~Interest on loans~~	**~~10%~~**
~~Interest due investors~~	**~~8%~~**
~~Investors share~~	**~~90%~~**
~~Target credit enhancement account (% of ending principal)~~	**~~5%~~**
~~Est. chargeoffs (per year, except 50% higher in year 5)~~	**~~3.5%~~**
~~Est. prepays (per year, after year 1)~~	**~~10%~~**

Servicing Assets and Servicing Liabilities

Adequate Compensation

78. *Q*—Paragraph 62 states that "typically, the benefits of servicing are expected to be more than *adequate compensation* to a servicer for performing the servicing . . ." (emphasis added). What is meant by the term *adequate compensation?*

 A—Paragraph 364 defines *adequate compensation* as "the amount of benefits of servicing that would fairly compensate a substitute servicer should one be required, which includes the profit that would be demanded in the marketplace." Adequate compensation is the amount of contractually specified servicing fees and other benefits of servicing that are demanded by the marketplace to perform the specific type of servicing. *Adequate compensation is determined by the marketplace; it does not vary according to the specific servicing costs of the servicer.* Therefore, a servicing contract that entitles the servicer to receive benefits of servicing just equal to adequate compensation, regardless of the servicer's own servicing costs, does not result in recognizing a servicing asset or a servicing liability. A servicer should record a~~n~~ servicing asset if the benefits of servicing exceed adequate compensation and a servicing liability if the benefits of servicing are less than adequate compensation. [Revised 6/09.]

79. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the fair value practicability exception.]

 ~~*Q*—If it is not practicable to determine adequate compensation, would it be acceptable to use the servicer's cost plus a profit margin to estimate the fair value of a servicing asset or liability for which a quoted market price is not available?~~

 ~~*A*—No. If it is not practicable to determine adequate compensation and a quoted market price is not available, then it is not practicable to determine fair value. In those circumstances, a transferor should refer to paragraph 71 for guidance. Refer to Question 80.~~

80. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the fair value practicability exception and Statement 157 defines fair value and establishes a framework for measuring fair value.]

 ~~*Q*—Does the response to Question 79 mean that an entity is precluded from using a cash flow model to estimate adequate compensation?~~

 ~~*A*—No. As explained in paragraph 71, if a quoted market price is not available, an entity should use a valuation technique such as a cash flow model to estimate the fair value of servicing unless it is not practicable to do so. Question 79 describes a situation in which the entity making the estimate has determined that it is not practicable to estimate adequate compensation using market assumptions. Adequate compensation is one of two amounts[16] that must be determined to measure the fair value of servicing. Therefore, it is not practicable to estimate the fair value of servicing if an entity cannot estimate adequate compensation.~~

81. [Deleted 6/09 because Statement 157 defines fair value and establishes a framework for measuring fair value.]

 ~~*Q*—Assume that a transferor undertakes an obligation to service mortgage loans that it originated and subsequently sold. The transferor believes that the benefits of that servicing slightly exceed "adequate compensation" and, therefore, that a small servicing asset should be recorded. However, on the date of the sale, the servicer receives an unsolicited bid from a third-party servicer that is a major market participant to purchase the right to service for a much larger sum. After due diligence, the transferor determines that the bid is legitimate. Which amount, the transferor's earlier estimate of fair value or the amount of the bid, should be the basis for the initial measurement of the servicing asset? [Revised 3/06.]~~

 ~~*A*—Paragraphs 13 and 62 of Statement 140 require that a separately recognized servicing asset be initially measured at its fair value. The transferor should use the unsolicited bid from the third party as the basis for determining the~~

~~[16]The other amount is the estimate of the benefits of servicing.~~

~~fair value of servicing as it represents a quoted market price for its asset. Paragraph 68 of Statement 140 states that "*if a quoted market price is available,* the fair value is the product of the number of trading units times that market price" (emphasis added). [Revised 3/06.]~~

82. [Deleted 6/09 because Statement 157 defines fair value and establishes a framework for measuring fair value.]

~~*Q*—Assume that a transferor undertakes an obligation to service loans that it originated and subsequently sold. In connection with that transaction, the transferor believes that the benefits of servicing exactly equal adequate compensation and, therefore, no servicing asset or liability should be recorded. To substantiate its assertion and because the market is shallow, the transferor contacts a broker and asks it to provide an estimate of the value of the transferor's servicing. The broker estimates that the transferor's servicing has substantial value (that is, the servicing should be recorded as a significant asset) but does not make or transmit a bid. How should the fair value of servicing be determined? [Revised 3/06.]~~

~~*A*—As discussed in Question 81, paragraphs 13 and 62 of Statement 140 require that a separately recognized servicing asset be initially measured at its fair value. Quoted market price in active markets is the best evidence of fair value. If a quoted market price is not available, the estimate of fair value shall be based on the best information available in the circumstances. This question highlights the potential for significantly different estimates of fair value of servicing when a quoted market price in an active market is not available. The difference between the two estimates suggests a need to perform more analysis to determine the best estimate of fair value. [Revised 3/06.]~~

~~Paragraph 68 of Statement 140 states that "quoted market prices in active markets are the best evidence of fair value and shall be used as the basis for the measurement, if available." However, an estimate of fair value (that is not a bid) from a single third party in an inactive or shallow market does not constitute a quoted market price even though it raises questions about the reasonableness of the transferor's estimated fair value of zero. The objective for any estimate of fair value is to determine "the amount at which that asset (or liability) could be bought (or incurred) or sold (or settled) in a current transaction between willing parties, that is, other than in a forced or liquidation sale" (paragraph 68). The transferor should analyze all available facts and circumstances, including the information provided by the broker about its estimate of the value of the transferor's servicing asset, in determining its best estimate of the fair value of the servicing contract. Some factors to consider include:~~

- ~~The legitimacy of the offer~~
- ~~The third party's specific knowledge about factors relevant to the fair value estimate~~
- ~~The experience of the broker in purchases of similar servicing contracts~~
- ~~Whether other parties have demonstrated interest in purchasing the servicing contract at a similar price.~~

~~[Revised 3/06.]~~

83. [Deleted 6/09 because Statement 157 defines fair value and establishes a framework for measuring fair value.]

~~*Q*—Assume an entity estimates the fair value of a servicing asset or liability by estimating the benefits of servicing and adequate compensation and comparing those amounts, as described in paragraph 62. Based on that estimate, the entity believes the value of the servicing is X. However, the entity obtains a quoted market price of Y. Which amount should the transferor use as its fair value for the servicing asset (or liability)?~~

~~*A*—The quoted market price. Paragraphs 68–70 explain how to determine fair value under Statement 140. Paragraph 69 explains that an estimate of fair value shall be made only when a quoted market price is not available (refer to Questions 81 and 82). The fact that the estimate of fair value is not the same as the quoted market price suggests that the model used to make the estimate may be flawed or the assumptions may be inappropriate.~~

~~The goal when estimating the value of servicing is to determine fair value (that is, what the market would pay or charge to assume servicing). Therefore, when estimating the benefits~~

~~of servicing, the benefits that should be included in the estimation model are those benefits that the market would consider, to the extent that the market would consider them. Similarly, when estimating adequate compensation, the estimated costs of servicing should be representative of those costs in the marketplace and should include a profit assumption equal to the profit demanded in the marketplace.~~

84. [Deleted 6/09 because Statement 157 defines fair value and establishes a framework for measuring fair value.]

~~*Q*—Assume that the quoted market price for servicing is lower than a transferor's estimate of fair value at the date of, and subsequent to, a transfer of assets in which the transferor retains those servicing rights. Can the transferor use the *quoted market price* to determine fair value when measuring the initial recognition amount and use its *estimate of fair value* when subsequently measuring impairment, if any?~~

~~*A*—No. Paragraphs 6870 explain how to determine fair value under Statement 140. Paragraph 69 explains that an estimate of fair value shall be made only when a quoted market price is not available (refer to Questions 81 and 82). The fact that the estimate of fair value is not the same as the quoted market price suggests that the model used to make the estimate may be flawed or the assumptions may be inappropriate. That fact should be taken into account in subsequent estimates of fair value if quoted market prices are not available. Refer to Question 83.~~

85. [Deleted 6/09 because Statement 157 defines fair value and establishes a framework for measuring fair value.]

~~*Q*—To what extent should benefits other than contractually specified fees, such as late charges and other ancillary revenue, be considered when valuing servicing assets and servicing liabilities?~~

~~*A*—Paragraph 364 defines *benefits of servicing* as "revenues from contractually specified servicing fees, late charges, and other ancillary sources, including 'float.'" The extent to which late charges and other ancillary revenue should be considered when determining the fair value of servicing should be consistent with the emphasis that the marketplace would place on such benefits when acquiring the obligation to service the underlying assets.~~

86. [Deleted 6/09 because Statement 157 defines fair value and establishes a framework for measuring fair value.]

~~*Q*—When estimating the fair value of servicing assets and liabilities, with regard to the benefits of servicing that are dependent on future transactions such as collecting late charges, should an entity estimate the value of *the right* to benefit from those potential transactions? Alternatively, should an entity estimate the value of the expected cash flows to be derived from those future transactions?~~

~~*A*—The entity should estimate the value of *the right* to benefit from the cash flows of potential future transactions, *not* the value of the expected cash flows to be derived from future transactions.~~

~~When estimating the fair value of servicing assets and liabilities, the goal is to estimate the "amount at which that asset (or liability) could be bought (or incurred) or sold (or settled) in a current transaction between willing parties . . ." (paragraph 68). A potential servicer might be willing to pay more for servicing if the benefits of that servicing included *the right* to collect late charges than it would pay if the benefits of servicing did not include those rights.~~

87. *Q*—For sales of mortgage loans, is adequate compensation the same as normal servicing fees previously used in applying Statement 65?

A—No. Paragraph 364 of Statement 140 defines *adequate compensation* as "the amount of benefits of servicing that would fairly compensate a substitute servicer should one be required, which includes the profit that would be demanded in the marketplace."

Prior to being amended by Statement 140, Statement 65 defined the term *current (normal) servicing fee rate* (normal servicing rate) as "a servicing fee rate that is representative of servicing fee rates most commonly used in comparable servicing agreements covering similar types of mortgage loans." Therefore, under Statement 65, normal servicing rates were based on the amounts most commonly charged for servicing a specific type of mortgage loan. The normal servicing rate was *not* used in estimating the aggregate initial carrying amount of servicing assets under the provisions of Statement 65, as amended by FASB Statement No. 122, *Accounting for Mortgage Servicing Rights.* Instead, it ensured that the amounts attributed to normal servicing activities were consistent among servicers of similar assets by designating contractually specified servicing rates above normal as *excess servicing.*

Often, a *normal servicing rate,* as that term was previously applied in practice under Statement 65, would result in more than *adequate compensation,* as that term is used in Statement 140. As a result, a purchaser often would be required to compensate a seller to obtain the right to service loans for a normal servicing rate. In contrast, a purchaser would neither pay nor receive payment to obtain the right to service for a rate just equal to adequate compensation.

88. *Q*—Do the types of assets being serviced affect the amount required to adequately compensate the servicer?

A—Yes. Several variables, including the nature of the underlying assets, should be considered in determining whether a servicer is adequately compensated. For example, the amount of effort required to service a home equity loan likely would be different from the amount of effort required to service a credit card receivable or a small business administration loan. Therefore, entities should consider the nature of the assets being serviced as a factor in determining the fair value of a servicing asset or servicing liability. [Revised 6/09.]

89. *Q*—Does a contractual provision that specifies the amount of servicing fees that would be paid to a replacement servicer affect the determination of adequate compensation?

A—No. The amount that would be paid to the replacement servicer under the terms of the servicing contract can be more or less than adequate compensation. The determination of whether the servicer is adequately compensated for servicing specified assets is based on the amount demanded by the marketplace, not the contractual amount to be paid to a replacement servicer. However, that contractual provision would be relevant for determining the amount of *contractually specified servicing fees,* which are defined in paragraph 364 as:

> All amounts that, per contract, are due to the servicer in exchange for servicing the financial asset and would no longer be received by a servicer if the beneficial owners of the serviced assets (or their trustees or agents) were to exercise their actual or potential authority under the contract to shift the servicing to another servicer. Depending on the servicing contract, those fees may include some or all of the difference between the interest rate collectible on the financial asset being serviced and the rate to be paid to the beneficial owners of those financial assets. [Revised 6/09.]

90. *Q*—If market rates for servicing a specific type of financial asset change subsequent to the initial recognition of a servicing asset or servicing liability, does Statement 140 include any requirement to adjust the recorded servicing asset or servicing liability? [Revised 6/09.]

A—Yes, in certain circumstances. Paragraphs 13A and 63 address the subsequent measurement of servicing assets and servicing liabilities. Under paragraphs 13A and 63, if an entity elects to subsequently measure a class of servicing assets and servicing liabilities using the fair value measurement method, changes in fair value are reported in earnings in the period in which the changes occur. If an entity elects to subsequently measure a class of servicing assets and servicing liabilities using the amortization method, each stratum within that class should be evaluated for impairment or increased obligation at each balance sheet date. If subsequent events increase the fair value of a stratum of servicing liabilities within a class that an entity has elected to subsequently measure using the amortization method, that increase must be recognized in earnings as a loss. [Revised 3/06.]

91. *Q*—Do additional transfers under revolving-period securitizations (for example, home equity loans or credit card receivables) result in the recognition of additional servicing assets or servicing liabilities? [Revised 6/09.]

A—Yes. Paragraph 78 states that "as new receivables are sold, rights to service them may become assets or liabilities ~~and~~ that are recognized." [Revised 6/09.]

Contractually Specified Servicing Fees

92. [Question deleted 3/06 because FASB Statement No. 156, *Accounting for Servicing of Financial Assets,* provides specific guidance that addresses this question in its amendment to paragraph 13 of Statement 140.]

93. *Q*—How should an entity account for rights to future income from serviced assets *that exceed contractually specified servicing fees?*

A—Paragraph 63 requires a servicing asset, an interest-only strip, or both to be recorded by a servicer if the benefits of servicing are expected to *exceed adequate compensation* for performing the servicing. It also states that a servicer should account for rights to receive future interest income from serviced assets *that exceed contractually specified servicing fees* separately from servicing assets. Those rights are not servicing assets; they are financial assets, effectively interest-only strips, that should be accounted for in accordance with paragraph 14.

Whether a right to future interest income should be accounted for as an interest-only strip, a servicing asset, or a combination thereof, depends on whether a servicer would continue to receive that amount (that is, the value of the right to future interest income) if a substitute servicer began servicing the assets. ~~Paragraph 287 states that ". . . i~~Interest-only strips obtained ~~retained~~ in securitizations ~~. . .~~ do not depend on the servicing work being performed satisfactorily, ~~[and]~~ are subsequently measured differently from servicing assets that arise from the same securitizations.~~"~~ Therefore, any portion of the right to future interest income from the serviced assets that would continue to be received even if the servicing were shifted to another servicer would be reported separately as a financial asset in accordance with paragraph 14. [Revised 6/09.]

94. *Q*—Should a loss be recognized if a servicing fee that is equal to or greater than adequate compensation is to be received but the servicer's anticipated cost of servicing would exceed the fee?

A—No. Whether a servicing asset or servicing liability is recorded is a function of the marketplace, not the servicer's cost of servicing. Paragraph 62 of Statement 140 explains:

> Typically, the benefits of servicing are expected to be more than adequate compensation to a servicer for performing the servicing, and the contract results in a servicing asset. However, if the benefits of servicing are not expected to adequately compensate a servicer for performing the servicing, the contract results in a servicing liability.

[Revised 3/06.]

Paragraph 364 of Statement 140 defines *adequate compensation* as "the amount of benefits of servicing that would fairly compensate a substitute servicer should one be required, which includes the profit that would be demanded in the marketplace." The guidance in those two paragraphs does not consider the servicer's cost of servicing. Furthermore, the impairment provisions of paragraphs 63(f) and 63(g) of Statement 140 for classes of servicing assets and servicing liabilities subsequently measured using the amortization method are based on the fair value of the contract rather than the gain or loss from subsequently carrying out the terms of the contract; future losses may be avoided by selling the servicing to a more efficient servicer. Statement 140 supersedes paragraph 11 and footnote 4 of Statement 65, which were based on a "loss contract" accounting approach—instead of the market-based approach required by Statement 140. [Revised 3/06.]

Servicing—Other

95. *Q*—Should an entity recognize a servicing liability if it transfers all or some of a financial asset that meets the definition of a participating interest ~~(for example, a loan participation)~~ that is accounted for as a sale and undertakes an obligation to service the financial asset but is not entitled to receive a contractually specified servicing fee? Is the answer to this question affected by circumstances in which it is not customary for the transferor-servicer to receive a contractually specified servicing fee? [Revised 3/06; 6/09.]

A—The transferor-servicer would be required to recognize a servicing liability at fair value if the benefits of servicing are less than adequate compensation. Paragraph 13 of Statement 140, as amended by Statement 166, states:

> An entity shall recognize and initially measure at fair value~~, if practicable,~~ a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in either ~~any~~ of the following situations:
>
> a. A servicer's transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset ~~the servicer's financial assets~~ that meets the requirements for sale accounting; or
>
> ~~b. A transfer of the servicer's financial assets to a qualifying SPE in a guaranteed mortgage securitization in which the transferor retains all of the resulting securities and classifies them as either available-for-sale securities or trading securities in accordance with FASB Statement No. 115,~~ ~~*Accounting for Certain Investments in Debt and Equity Securities*~~
>
> c. An acquisition or assumption of a servicing obligation that does not relate to financial assets of the servicer or its consolidated affiliates included in the financial statements being presented.
>
> An entity that transfers its financial assets ~~to a qualifying SPE in a guaranteed mortgage securitization~~ to an unconsolidated entity in a transfer that qualifies as a sale in which the transferor ~~retains all of~~ obtains the resulting securities and classifies them as debt securities held-to-maturity in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* may either separately recognize its servicing assets or servicing liabilities or report those servicing assets or servicing liabilities together with the asset being serviced.

[Revised 3/06; 6/09.]

Those requirements apply even if it is not customary to charge a contractually specified servicing fee. Paragraph 62 of Statement 140 states that ". . . if the benefits of servicing are not expected to adequately compensate a servicer for performing the servicing, the contract results in a servicing liability." [Revised 3/06.]

96. *Q*—Assuming that (a) an entity transfers a portion of a loan under a participation agreement that meets the definition of a participating interest and qualifies for sale accounting under Statement 140, (b) the selling entity obtains the right to receive benefits of servicing that more than adequately compensate it for servicing the loan, and (c) the selling entity would continue to service the loan, regardless of the transfer because it retains part of the participated loan, is the selling entity required to record a servicing asset? [Revised 6/09.]

A—Yes. The selling entity would be required to record a servicing asset for the portion of the loan~~s~~ it sold (paragraph 62 of Statement 140). The assumption that the selling entity would service the loan because it retains part of the participated loan does not impact the requirement to recognize a servicing asset. Conversely, a selling entity could not avoid recording a servicing liability if the benefits of servicing are not expected to adequately compensate the servicer for performing the servicing. However, if the benefits of servicing are significantly above an amount that would fairly compensate a substitute service provider, should one be required, the transferred portion does not meet the definition of a participating interest, and, therefore, the transfer does not qualify for sale accounting (paragraph 8B(b)). [Revised 3/06; 6/09.]

97. *Q*—A~~n~~ transferor ~~entity~~ sells mortgage loans in their entirety that it has originated in a transfer that is accounted for as a sale and undertakes an obligation to service them. Immediately thereafter, the transferor ~~entity~~ enters into an arrangement to subcontract the obligation to service with another servicer. How should the transferor ~~entity~~ account for the obligation to service as a result of those transactions? [Revised 3/06; 6/09.]

A—The transferor ~~entity~~ should account for the two transactions separately. First, the transferor ~~entity~~ should account for the sale ~~transfer~~ of mortgage loans and its obligation to service the loans in accordance with paragraphs 11–13B of Statement 140, as amended by Statement 166—the obligation to service should be initially recognized and measured at fair value~~,~~ ~~if practicable~~, according to paragraph~~s 10 and~~ 11 of Statement 140 as proceeds obtained from the sale ~~transfer~~ of the mortgage loans. Second, the transferor ~~entity~~ should account for the subcontract with another servicer. The transferor's accounting for the latter transaction is not within the scope of Statement 140 because servicing assets are not financial assets and paragraph 4 states that Statement 140 does not address transfers of nonfinancial assets.~~it does *not* involve a *transfer* of the underlying mortgage loans and, therefore,~~ Therefore, the transferor's accounting for the latter transaction should be accounted for under other existing guidance (SOP 01-6 and Issue 95-5). [Revised 3/06; 6/09.]

98. *Q*—When servicing assets are assumed without cash payment, what is the appropriate offsetting entry by the transferee?

A—The answer depends on whether an exchange or capital transaction has occurred.

If an exchange has occurred, then the transaction should be recorded based on the facts and circumstances. For example, the servicing asset may represent consideration for goods or services provided by the transferee to the transferor of the servicing. In that case, the offsetting entry by the transferee would be the same as if cash was received in exchange for the goods and services (that is, revenue or a liability as appropriate).~~[17]~~ The servicing assets also might be received in full or partial satisfaction of a receivable from the transferor of the servicing. In those cases, the offsetting entry by the transferee would be to derecognize all or part of the receivable satisfied in the exchange. [Revised 6/09.]

Another possibility is that an investor is in substance making a capital contribution to the investee (the party receiving the servicing [that is, the transferee]) in exchange for an increased ownership interest. In that case, the investee should recognize an increase in equity from a contribution by owner.

~~It is difficult to envision scenarios in which a servicing asset would be assumed without cash payment or other consideration in an exchange or a capital transaction. In those scenarios, it is possible that the value of the servicing has been overstated by the transferee. Therefore, those scenarios should be carefully scrutinized for changes in terms, restrictions on sale, and so forth, that may indicate that the value of the servicing has been overstated.~~

99. *Q*—Statement 140 requires that entities separately evaluate and measure impairment of designated strata of servicing assets within classes of servicing assets that are subsequently measured using the amortization method. Must those classes of servicing assets be stratified based on more than one predominant risk characteristic of the underlying financial assets if more than one characteristic exists? [Revised 3/06.]

A—No. Paragraph 13A of Statement 140 requires that an entity subsequently measure each class of servicing assets and servicing liabilities using either the amortization method or the fair value method. Paragraph 63(f)(1) of Statement 140 requires servicers to "stratify servicing assets within a class based on *one or more* of the predominant risk characteristics of the underlying financial assets" (emphasis added) for classes of servicing assets that a servicer elects to subsequently measure using the amortization method. Therefore, Statement 140 does not require that either the most predominant risk characteristic or more than one predominant risk characteristic be used to stratify the servicing assets for purposes of evaluating and measuring impairment. A servicer must exercise judgment when determining how to stratify servicing assets (that is, when selecting the most appropriate characteristic(s) for stratification). [Revised 3/06.]

Pursuant to paragraph 56 of Statement 133, "at the date of initial application, mortgage bankers and other servicers of financial assets may

~~[17]To the extent the apparent value of the servicing asset exceeds the value of the cash that would have been recieved had the transaction been consummated as a cash transaction, it is likely that the fair value of the servicing has been overstated.~~

choose [but are not required] to restratify[18] their servicing rights pursuant to paragraph 63(f) of Statement 140 in a manner that would enable individual strata to comply with the requirements of this Statement [133] regarding what constitutes 'a portfolio of similar assets.'" An entity may use different stratification criteria for the purposes of Statement 140 impairment testing and for the purposes of grouping similar assets to be designated as a hedged portfolio in a fair value hedge under Statement 133. [Revised 3/06; 6/09.]

100. *Q*—Paragraph 63(f)(1) of Statement 140 requires a servicer to "stratify servicing assets within a class based on one or more of the predominant risk characteristics of the underlying financial assets" for classes of servicing assets that a servicer elects to subsequently measure using the amortization method. Should the stratums selected by the servicer be used consistently from period to period? [Revised 3/06.]

A—Generally, yes. Once an entity has determined the predominant risk characteristics to be used in identifying the resulting stratums within each class of servicing assets subsequently measured using the amortization method, that decision should be applied consistently unless significant changes in economic facts and circumstances clearly indicate that the predominant risk characteristics and resulting stratums should be changed. If a significant change in economic facts and circumstances occurs, that change should be accounted for prospectively as a change in accounting estimate in accordance with paragraphs 19–22 of FASB Statement No. 154, *Accounting Changes and Error Corrections.* If the predominant risk characteristics and resulting stratums are changed, that fact and the reasons for those changes should be included in the disclosures about the risk characteristics of the underlying financial assets used to stratify the recognized servicing assets in accordance with paragraph 17(~~g~~e)(~~4~~3) of Statement 140. [Revised 3/05; 3/06; 6/09.]

101. *Q*—Statement 140 requires impairment of servicing assets to be recognized "through a *valuation allowance* for an individual stratum" (paragraph 63(f)(2); emphasis added) for classes of servicing assets that a servicer elects to subsequently measure using the amortization method. The *valuation allowance* should "reflect changes in the measurement of impairment subsequent to the initial measurement of impairment. Fair value in excess of the carrying amount of servicing assets for that stratum, however, shall not be recognized" (paragraph 63(f)(3)). How should an entity recognize subsequent increases in a previously recognized *servicing liability?* [Revised 3/06.]

A—Paragraph 63(g) of Statement 140 states that "for servicing liabilities subsequently measured using the amortization method, if subsequent events have increased the fair value of the liability above the carrying amount, for example, because of significant changes in the amount or timing of actual or expected future cash flows relative to the cash flows previously projected, the servicer shall revise its earlier estimates and recognize the increased obligation as a loss in earnings." Similar to the accounting for changes in a valuation allowance for an impaired asset, increases in the servicing obligation may be recovered, but the obligation should not be reduced below the amortized measurement of the initially recognized servicing liability. If an entity makes an election to subsequently measure a class of servicing liabilities using the fair value measurement method, any changes in fair value should be reported in earnings in the period in which those changes occur. [Revised 3/06.]

102. [Deleted 6/09 because Statement 140, as amended by Statement 166, removes the fair value practicability exception.]

~~*Q*—Assume that a transferor transfers financial assets and undertakes an obligation to service those financial assets. If it is not practicable for a transferor to measure the fair value of servicing at the date of transfer, is the transferor required to evaluate whether its obligations under the servicing agreement represent a liability?~~

~~*A*—Yes. When applying paragraph 71, the transferor must evaluate whether a liability has been incurred as a result of its obligations under~~

[18]That restratification of servicing rights is a change in the application of an accounting principle. Paragraph 56 of Statement 133 provides guidance on accounting for that change.

~~the servicing agreement and should not automatically assume that an asset exists (that is, not automatically assume that the answer is zero).~~

103. [Deleted 6/09 because Statement 157 defines fair value and establishes the framework for measuring fair value.]

~~*Q*—Should a valuation technique using undiscounted cash flows ever be used to estimate fair value of servicing liabilities?~~

~~*A*—No. A valuation technique that includes discounting should be used to estimate fair value. Using a valuation technique that does not consider the time value of money (discounting) would be inconsistent with the notion of fair value as described in paragraphs 68–70. Further, paragraph 69 explains that when measuring "servicing liabilities at fair value, the objective is to estimate the value of the assets required currently to (a) settle the liability with the holder or (b) transfer a liability to an entity of comparable credit standing."~~

Financial Assets Subject to Prepayment

104. *Q*—If an entity recognizes both a servicing asset and the right to receive future interest income from serviced assets in excess of contractually specified servicing fees (an interest-only strip) in a transfer of an entire financial asset to an unconsolidated entity that meets the requirements for sale accounting, should the value of the *right to* receive future cash flows from ancillary sources such as late fees be included in measuring the servicing asset or in measuring the interest-only strip? [Revised 6/09.]

A—Generally, in the servicing asset. The value of the right to receive future cash flows from ancillary sources such as late fees is included in the measurement of the servicing asset, not the interest-only strip, if retention of the right to receive the cash flows from those fees depends on servicing being performed satisfactorily, as is generally the case. When valuing that right, the entity should estimate the value of the right to benefit from the cash flows of potential future transactions, not the value of the expected cash flows to be derived from future transactions. ~~As discussed in paragraph 287, a~~An interest-only strip does not depend on servicing being performed satisfactorily. [Revised 6/09.]

105. *Q*—Paragraph 14 requires that ~~interest-only strips and similar~~ financial assets, except for instruments that are within the scope of Statement 133, that can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment subsequently be measured like investments in debt securities classified as available-for-sale or trading under Statement 115. Does that requirement result in those financial assets being included in the scope of Statement 115? [Revised 6/09.]

A—Whether those financial assets are included in the scope of Statement 115 depends on the form of the assets. However, in either case, the measurement principles of Statement 115, including the provisions for recognizing and measuring impairment, should be applied.

Interest-only strips and similar interests ~~that continue to be held by a transferor~~ that meet the definition of *securities* in paragraph 137 of Statement 115 are included in the scope of Statement 115; therefore, all relevant provisions of that Statement (for example, the disclosures) should be applied. Those interests should be classified as available-for-sale or trading pursuant to the provisions of paragraph 7 of Statement 115, as amended by paragraph 362 of Statement 140. [Revised 3/06; 6/09.]

Interest-only strips and similar interests ~~that continue to be held by a transferor~~ that are not in the form of securities (as defined in Statement 115) are not within the scope of Statement 115 but should be *measured* like investments in debt securities classified as available-for-sale or trading. In that case, all of the measurement provisions, including those addressing recognition and measurement of impairment, should be followed. However, other provisions of Statement 115, such as those addressing disclosures, are not required to be applied. [Revised 3/06; 6/09.]

106. *Q*—Can a financial asset that can be contractually prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment be classified as held-to-maturity if the investor concludes that prepayment or other forms of settlement are *remote?*

A—No. The probability of prepayment or other forms of settlement that would result in the holder's not recovering substantially all of its recorded investment is not relevant in deciding whether the provisions of paragraph 14 apply to those financial assets. [Revised 6/09.]

107. *Q*—A transferor transfers mortgage loans in their entirety to a third party in a transfer that is accounted for as a sale but undertakes an obligation to service the loans. Subsequent to the transfer, the transferor enters into a subservicing arrangement with a third party. If the transferor's benefits of servicing exceed its obligation under the subservicing agreement, should that differential be accounted for as an interest-only strip? [Revised 3/06; 6/09.]

A—No. The transferor ~~entity~~ should account for the two transactions separately. First, the transferor ~~entity~~ should account for the transfer of mortgage loans and its obligation to service the loans in accordance with Statement 140. [Revised 6/09.]

Paragraph 13 of Statement 140 states that:

> An entity shall recognize and initially measure at fair value~~, if practicable,~~ a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in either ~~any~~ of the following situations:
>
> a. A servicer's transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset ~~the servicer's financial assets~~ that meets the requirements for sale accounting; or
>
> ~~b. A transfer of the servicer's financial assets to a qualifying SPE in a guaranteed mortgage securitization in which the transferor retains all of the resulting securities and classifies them as either available-for-sale securities or trading securities in accordance with FASB Statement No. 115,~~ ~~*Accounting for Certain Investments in Debt and Equity Securities*~~
>
> c. An acquisition or assumption of a servicing obligation that does not relate to financial assets of the servicer or its consolidated affiliates included in the financial statements being presented.
>
> An entity that transfers its financial assets ~~to a qualifying SPE in a guaranteed mortgage securitization~~ to an unconsolidated entity in a transfer that qualifies as a sale in which the transferor ~~retains all of~~ obtains the resulting securities and classifies them as debt securities held-to-maturity in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* may either separately recognize its servicing assets or servicing liabilities or report those servicing assets or servicing liabilities together with the asset being serviced.

[Revised 3/06; 6/09.]

The obligation to service should be initially recognized and measured at fair value as proceeds obtained from the sale of the mortgage loans~~, if practicable,~~ according to paragraphs ~~10 and~~ 11 of Statement 140, as amended by Statement 166. Second, the transferor ~~entity~~ should account for the contract with the subservicer. The transferor's accounting for the latter transaction is not within the scope of Statement 140 because servicing assets and servicing liabilities are not financial assets, and paragraph 4 of Statement 140 states that *that* Statement does not address transfers of nonfinancial assets. ~~it does *not* involve a *transfer* of the underlying mortgage loans and, therefore,~~ Therefore, the transferor's accounting for the latter transaction should be accounted for under other existing guidance (SOP 01-6 and Issue 95-5). Refer to Question 97. [Revised 3/06; 6/09.]

108. *Q*—Can a debt security that is purchased late enough in its life such that, even if it was prepaid, the holder would recover substantially all of its recorded investment, be initially classified as held-to-maturity?

A—Yes. The debt security could be initially classified as held-to-maturity if the conditions of paragraph 7 of Statement 115 are met. Paragraph 7 allows that classification "only if the reporting enterprise has the positive intent and ability to hold those securities to maturity." Paragraph 362 of Statement 140 added the following requirement to the end of paragraph 7 of Statement 115: "A [debt] security may not be classified as held-to-maturity if that security can contractually be prepaid or otherwise settled in such a way that the holder of the [debt] security would not recover substantially all of its recorded investment."

109. *Q*—May a loan (that is not a debt security) that when initially obtained ~~acquired or retained~~ could be contractually prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment be reclassified as held for investment later in its life (that is, at a date that is so close to the financial asset's maturity that the holder would recover substantially all of its recorded investment even if it was prepaid)? In other words, would that loan no longer be required to be measured in accordance with the guidance in paragraph 14 of Statement 140? [Revised 6/09.]

A—Yes, if (a) it would no longer be possible for the holder not to recover substantially all of its recorded investment upon contractual prepayment or settlement and (b) the conditions for amortized cost accounting are met (for example, paragraph 6 of Statement 65 and paragraph~~s~~ .08(a) of SOP 01-6~~6.48 and 6.49 of the May 1, 2000 AICPA Audit and Accounting Guide, *Banks and Savings Institutions*~~). However, any unrealized holding gain or loss arising under the available-for-sale classification that exists at the date of the reclassification would continue to be reported in other comprehensive income but should be amortized over the remaining life of the loan as an adjustment of yield. (The loan would not be classified as held-to-maturity because under Statement 115 and its interpretations, only debt securities may be classified as held-to-maturity.) [Revised 6/09.]

110. *Q*—Paragraph 14 requires that certain financial assets that are not in the form of debt securities be measured at fair value like investments in debt securities classified as available-for-sale or trading under Statement 115. How should instruments subject to the provisions of paragraph 14 be evaluated for impairment?

A—All of the measurement provisions of Statement 115, including recognition and measurement of impairment, should be applied to those financial assets. Further, other existing literature that interprets Statement 115 should be applied, as appropriate, to financial assets within the scope of paragraph 14. (See Question 122.) For example, Issue 99-20 and FSP EITF 99-20-1, *Amendments to the Impairment Guidance of EITF Issue No. 99-20,* provide~~s~~ guidance on how to apply the impairment provisions of Statement 115 to financial assets that are within the scope of Issue 99-20. [Revised 6/09.]

111. *Q*—Is a financial asset that is not a debt security under Statement 115 subject to the requirements of paragraph 14 because it is denominated in a foreign currency?

A—No. An entity is not required to measure such an investment like a debt security under paragraph 14 unless it has provisions that allow it to be contractually prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment, as denominated in the foreign currency. For example, an investment denominated in deutsche marks by an entity with a U.S. dollar functional currency would not be subject to paragraph 14 if the contract requires that substantially all of the invested deutsche marks be repaid. Investing in a financial asset that is denominated in a foreign currency often exposes an entity to foreign currency exchange rate risk; however, that risk is not addressed in paragraph 14. Paragraph 295 explains that "the Board also concluded that the provisions of paragraph 14 do not apply to situations in which events that are not the result of contractual provisions, for example, borrower default or changes in the value of an instrument's denominated currency relative to the entity's functional currency, cause the holder not to recover substantially all of its recorded investment."

112. *Q*—Is a note for which the repayment amount is indexed to the creditworthiness of a party other than the issuer subject to the provisions of paragraph 14 (which precludes held-to-maturity classification)?

A—Yes. A note for which the repayment amount is indexed to the creditworthiness of a party other than the issuer is subject to the provisions of paragraph 14 because the event that might cause the holder to receive less than substantially all of its recorded investment is based on a contractual provision, not on a default by the borrower (that is, the issuer of the note). That contractual provision indexes the payment terms of the note to a default by a third party unrelated to the issuer of the note.

If that note is within the scope of Statement 133, the guidance of paragraph 14 of Statement 140 would not apply~~no longer apply because Statement 133 amended paragraph 14 of Statement 125 to exclude instruments subject to the provisions of Statement 133. Under Statement 133, the accounting likely will be different from the accounting under paragraph 14 of Statement 140~~. [Revised 6/09.]

113. *Q*—Can a residual tranche debt security in a securitization of financial assets (for example, receivables) using a ~~qualifying SPE~~ securitization entity be classified as held-to-maturity? [Revised 6/09.]

A—The answer depends on the facts and circumstances. If the contractual provisions of the residual tranche debt security provide that the residual tranche can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment, the residual tranche debt security *should not* be accounted for as held-to-maturity in accordance with paragraph 14. In contrast, if the only way that the holder of the residual tranche would not recover substantially all of its recorded investment would be in response to a default by the borrower (debtor), then a held-to-maturity classification is acceptable as long as the conditions specified for a held-to-maturity classification in paragraph 7 of Statement 115, as amended, have been met. ~~In that case, *the borrower is the issuer of the receivables held by the qualifying SPE after the transfer has occurred.*~~ [Revised 6/09.]

~~Paragraph 173 explains that "the effect of establishing the qualifying SPE is to merge the contractual rights in the transferred assets and to allocate undivided interests in them—the beneficial interests." Paragraph 273 elaborates on that effect by explaining that a transfer of assets to a qualifying SPE in a securitization changes the nature of the asset held by the transferor. [Revised 3/06.]~~

Paragraph 295 states that ". . . the rationale outlined in paragraph 293 extends to any situation in which a lender would not recover substantially all of its recorded investment if borrowers were to exercise prepayment or other rights granted to them under the contracts. The Board also concluded that the provisions of paragraph 14 do not apply to situations in which events that are not the result of contractual provisions, for example, *borrower default* or changes in the value of an instrument's denominated currency relative to the entity's functional currency, cause the holder not to recover substantially all of its recorded investment" (emphasis added).

Secured Borrowings and Collateral

114. *Q*—Are the collateral accounting requirements of paragraph 15 limited to transfers by or to broker-dealer entities, or do they apply to other types of borrowings, such as the origination of corporate debt and standard bank loans?

A—The collateral accounting provisions of paragraph 15 apply to all transfers of financial assets pledged as collateral in a transaction accounted for as a secured borrowing. Accordingly, they apply to many repurchase agreement, dollar-roll, securities lending, and similar transactions in which cash is obtained in exchange for financial assets with an obligation for an opposite exchange later, as well as to many other transactions. However, as noted in footnote 4 to paragraph 15 and in paragraph 94, those collateral accounting provisions do not apply to cash, or securities that can be sold or pledged for cash, received as so-called "collateral" for noncash financial assets, for example, in certain securities lending transactions. Such cash or securities that can be sold or pledged for cash are accounted for as proceeds of either a sale or a borrowing.

115. *Q*—What is the proper classification by the transferor of securities loaned or transferred under a repurchase agreement accounted for as a secured borrowing if the transferee is permitted to sell or repledge those securities?

A—Paragraph 15 provides guidance on collateral accounting issues. Paragraph 15(a) indicates that pledged assets should be reclassified in the statement of financial position separately from other assets not so encumbered. However, it does not specify the classification or the terminology to be used to describe those assets. Paragraph 95 illustrates possible classifications and terminology.

116. *Q*—What is the appropriate classification of liabilities incurred in connection with securities borrowing and resale agreement transactions?

A—Statement 140 does not specify classification or terminology to be used to describe liabilities incurred by either the secured party or debtor in securities borrowing or resale transactions. However, those liabilities should be separately classified. Paragraph 95 illustrates possible classifications and terminology.

117. *Q*—How should a transferor measure transferred collateral that must be reclassified (for example, as securities pledged to creditors)?

A—Paragraph 15(a) requires that transferred collateral that the secured party can, by contract or custom, sell or repledge be reclassified and reported separately by the transferor. That paragraph, however, does not change the transferor's measurement of that collateral. Because the transferor continues to effectively control the collateral, it should not derecognize the collateral and should follow the same measurement principles as before the transfer. For example, securities reclassified from the available-for-sale category to securities pledged to creditors should continue to be measured at fair value, with changes in fair value reported in comprehensive income, while debt securities reclassified from the held-to-maturity category to securities pledged to creditors should continue to be measured at amortized cost.

118. *Q*—Does Statement 140 provide guidance on subsequent measurement of a secured party's (transferee's) obligation to return transferred collateral that it recognized in accordance with paragraph 15?

A—No. Statement 140 generally does not address subsequent measurement of transferred financial assets or the obligation to return transferred collateral. The liability to return the collateral should be measured in accordance with other relevant accounting pronouncements. For example, a bank or savings institution that, as transferee, sells transferred collateral is required to subsequently measure that liability like a short sale at fair value. ~~Paragraph 5.93 of the AICPA Audit and Accounting Guide on banks and savings institutions states that "the obligations incurred in short sales should be reported as liabilities and adjusted to fair value through the income statement at each reporting date."~~Paragraph .10(b) of SOP 01-6 states that "the obligations incurred in short sales should be reported as liabilities and adjusted to fair value through the income statement at each reporting date" (footnote reference omitted). [Revised 6/09.]

Extinguishments of Liabilities

119. *Q*—Are liabilities extinguished by legal defeasances?

A—Yes, if the condition in paragraph 16(b) is satisfied. In a legal defeasance, generally the creditor legally releases the debtor from being the primary obligor under the liability. Whether the debtor has in fact been released and the condition in paragraph 16(b) has been met is a matter of law. Conversely, in an in-substance defeasance, the debtor is not released from the debt by putting assets in the trust—for that reason, and others identified in paragraph 311, an in-substance defeasance is different from a legal defeasance and the liability is not extinguished. ~~A related issue is discussed in Question 35.~~ [Revised 6/09.]

120. *Q*—How should a debtor account for the exchange of an outstanding debt instrument with a lender for a new debt instrument with the same lender but with substantially different terms? Other than as an exchange transaction, how should the debtor account for a substantial modification of a debt instrument?

A—Paragraph 16 permits derecognition of liabilities if and only if it is extinguished by one of the following conditions: the debtor pays the creditor and is relieved of its obligation or the debtor is legally released as the primary obligor, either judicially or by the creditor. The EITF addressed how a debtor should account for a substantial modification of a debt instrument in Issues No. 96-19, "Debtor's Accounting for a Modification or Exchange of Debt Instruments," and No. 98-14, "Debtor's Accounting for Changes in Line-of-Credit or Revolving-Debt Arrangements."

121. *Q*—If an entity is released from being primary obligor and becomes a secondary obligor, should the entity recognize the resulting guarantee (from being the secondary obligor) in the same manner as a third-party guarantor?

A—Yes. As stated in paragraph 114, the entity should recognize the guarantee "in the same manner as would a guarantor that had never been primarily liable to that creditor, with due regard for the likelihood that the third party will carry out its obligations. The guarantee obligation shall be initially measured at fair value, and that amount reduces the gain or increases the loss recognized on extinguishment."

Other

122. *Q*—Does Statement 140 address impairment of financial assets?

A—As discussed in paragraph 4, Statement 140 "does not address subsequent measurement of assets and liabilities, except for (a) servicing assets and servicing liabilities and (b) interest-only strips, ~~securities,~~ other beneficial interests ~~that continue to be held by a transferor in securitizations~~, loans, other receivables, or other financial assets that can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment. . . ." Accordingly, impairment of financial assets should be measured by reference to other applicable existing guidance, such as: [Revised 6/09.]

- FASB Statement No. 5, *Accounting for Contingencies*
- FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan* (as amended by FASB Statement No. 118, *Accounting by Creditors for Impairment of a Loan—Income Recognition and Disclosures*)
- Statement 115
- FASB Statement No. 134, *Accounting for Mortgage-Backed Securities Retained after the Securitization of Mortgage Loans Held for Sale by a Mortgage Banking Enterprise*
- FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments*
- FSP FAS 115-1 and FAS 124-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*
- FSP FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*
- Issue 99-20
- FSP EITF 99-20-1.
- ~~Related EITF Issues.~~

[Revised 3/06; 6/09.]

123. *Q*—Many securitization structures provide for a disproportionate distribution of cash flows to various classes of investors during the amortization period, which is referred to as a turbo provision. For example, a turbo provision might require the first $100 million of cash received during the amortization period of the securitization structure to be paid to one class of investors before any cash is available for repayment to other investors. Similarly, certain revolving-period securitizations use what is referred to as a *bullet* provision as a method of distributing cash to their investors. Under a bullet provision, during a specified period preceding liquidating distributions to investors, cash proceeds from the underlying assets are reinvested in short-term investments other than the underlying revolving-period receivables. Those investments mature or are otherwise liquidated to make a single bullet payment to certain classes of investors.

If the transfer consists of an entire financial asset or a group of entire financial assets to an unconsolidated entity, what ~~What~~ effect do such turbo and bullet provisions in securitization structures have on the accounting for the transfers of financial assets under Statement 140? [Revised 6/09.]

A—Under Statement 140, trust liquidation methods that allocate receipts of principal or interest between beneficial interest holders and transferors in proportions different from their stated percentage of ownership interests do not affect whether the transferor should obtain sale accounting and derecognize those transferred assets, assuming the trust is not required to be consolidated by the transferor. However, both ~~Both~~ turbo and bullet provisions should be taken into consideration~~, however,~~ in determining the ~~relative~~ fair values of ~~the portion of transferred assets sold and portions retained by the transferor~~assets obtained by the transferor and transferee. Refer to Question 49. [Revised 6/09.]

C3. This Statement nullifies the following EITF Issues and Topics:

a. EITF Issue No. 02-12, "Permitted Activities of a Qualifying Special-Purpose Entity in Issuing Beneficial Interests under FASB Statement No. 140"

b. EITF Topic No. D-66, "Effect of a Special-Purpose Entity's Powers to Sell, Exchange, Repledge, or Distribute Transferred Financial Assets under FASB Statement No. 125."

C4. The FASB has indicated that the following EITF Issues are not applicable in the *FASB Accounting Standards Codification*™. The Codification is expected to be effective before the effective date of this Statement:

a. EITF Issue No. 86-36, "Invasion of a Defeasance Trust"
b. EITF Issue No. 89-2, "Maximum Maturity Guarantees on Transfers of Receivables with Recourse"
c. EITF Issue No. 90-18, "Effect of a 'Removal of Accounts' Provision on the Accounting for a Credit Card Securitization"
d. EITF Issue No. 92-2, "Measuring Loss Accruals by Transferors for Transfers of Receivables with Recourse."

C5. The SEC staff has indicated that it will consider amending or nullifying the guidance in EITF Topic No. D-69, "Gain Recognition on Transfers of Financial Assets under FASB Statement No. 140," before the effective date of this Statement. Thus, that Topic does not reflect this Statement's amendments to Statement 140.

C6. This Statement amends the following EITF Issues and Topics.

C7. EITF Issue No. 84-5, "Sale of Marketable Securities with a Put Option," is amended as follows:

a. The second through ninth paragraphs of the STATUS section:

Statement 125 was issued in June 1996 and was replaced by Statement 140. Statement 140 provides accounting and reporting standards for transfers and servicing of financial assets and extinguishments of liabilities. Statement 166 was issued in June 2009 and amends Statement 140. ~~is effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after March 31, 2001. The effective dates for securitization disclosures and accounting for collateral are detailed in paragraphs 22 and 23 of Statement 140.~~

Issue 1— Statement 140, as amended by Statement 166, partially nullifies this consensus. Under Statement 140, as amended by Statement 166, sale accounting is precluded if a transferor maintains effective control over the transferred financial assets. Paragraph 9(c) of Statement 140 and the related implementation guidance in paragraphs 46A–54A, as amended by Statement 166, provide examples of when a transferor maintains effective control over transferred financial assets. ~~the existence of a put option or the probability that it will be exercised *may* affect the determination of whether a transfer qualifies for sale treatment but only if the marketable security is not readily obtainable. For example, put options written to the transferee generally do not constrain it, but a put option on a not-readily-obtainable asset may benefit the transferor and effectively constrain the transferee if the option is sufficiently deep in the money when it is written that it is probable that the transferee will exercise it and the transferor will reacquire the transferred asset. Neither~~ Statements 125, ~~nor Statement~~ 140, and 166 do not address subsequent measurement of put options entered into in a transaction accounted for as a sale. The measurement guidance in this consensus would be retained for transactions accounted for as secured borrowings.

Issue 2a— Statement 140, as amended by Statement 166, ~~partially~~ nullifies this consensus. Under Statement 140, as amended by Statement 166, sale accounting is precluded if a transferor maintains effective control over the transferred financial assets. Paragraph 9(c) of Statement 140 and the related implementation guidance in paragraphs 46A–54A, as amended by Statement 166, provide examples of when a transferor maintains effective control over transferred financial assets. ~~the existence of put option or the probability that it will be exercised *may* affect the determination of whether the transfer qualifies for sale~~

~~treatment but only if the marketable security is considered a financial asset that is not readily obtainable. For example, put options written to the transferee generally do not constrain it, but a put option on a not-readily-obtainable asset may benefit the transferor and effectively constrain the transferee if the option is sufficiently deep in the money when it is written that it is probable that the transferee will exercise it and the transferor will reacquire the transferred asset.~~

Issue 2b—Statement 140 nullifie~~d~~s the Task Force consensus that continual reassessment of the probability that the put option will be exercised is required. Under Statement 140, the assessment of the probability that the put option will be exercised and the transferee is constrained is required only at the transaction date. Statement 166 does not reconsider this matter.

Issue 3—Statement 125 partially nullified this consensus. Statements 140 and 166 ~~did~~ do not reconsider this matter. ~~Neither~~ Statements 125, ~~nor Statement~~ 140, and 166 do not address subsequent measurement of put options entered into in a transaction accounted for as a sale. If the security is subsequently repurchased, it would be recorded in accordance with Statement 115.

Issue 4—Statement 125 nullifies this consensus. Statements 140 and 166 do ~~did~~ not reconsider this matter. Under both Statement~~s~~ 125 and Statement 140, as amended by Statement 166, the remaining life of a put option does not affect the determination of whether the transfer qualifies for sale treatment.

Issue 5—Statement 125 partially nullified this consensus. Statements 140 and 166 do ~~did~~ not reconsider this matter. ~~Under both Statements 125 and 140, the existence of multiple put options would not affect the determination of whether the transfer qualifies for sale treatment. However, the~~Under Statement 140, as amended by Statement 166, sale accounting is precluded if a transferor maintains effective control over the transferred financial assets. The financial components approach requires the recognition of the multiple put options as liabilities, initially measured at fair value, for transfers qualifying for sale treatment. ~~Neither~~ Statements 125, ~~nor Statement~~ 140, and 166 do not address subsequent measurement of put options entered into in a transaction accounted for as a sale. The measurement guidance in this consensus would be retained for transactions accounted for as secured borrowings.

Issue 6—The issue of accounting for transactions involving possible gains was discussed by the Task Force separately in Issues 85-30 and 85-40 (Issue 5). ~~However, no consensus was reached.~~ Issue 85-30 was resolved by Statement 125, and Statement 125 nullified the consensus reached in Issue 5 of Issue 85-40. Statement 125 required recognition of liabilities (including put options) incurred as proceeds of a sale of a financial asset and initial measurement at fair value, if practicable. Statement 140 did not reconsider this matter. Statement 166, which was issued in June 2009 and amends Statement 140, removes the practicability exception for the requirement to initially measure proceeds of a sale at fair value.~~The accounting for sales of marketable securities with put arrangements was revisited in Issue 85-40. In that Issue, the Task Force reached a consensus that for transactions that would involve gains if reported as sales, the assets should be removed from the balance sheet, but the gain should be deferred because it represents a gain contingency that under Statement 5~~

~~should not be recognized until the contingency is resolved by expiration of the put option without exercise.~~

C8. EITF Issue No. 84-20, "GNMA Dollar Rolls," is amended as follows:

a. The fourth paragraph of the STATUS section:

This Issue was partially resolved by Statement 125, which was issued in June 1996. Statement 125 was replaced by Statement 140, without reconsideration of this matter. Statement 166, which was issued in June 2009, amends Statement 140 without reconsideration of this matter.

C9. EITF Issue No. 85-25, "Sale of Preferred Stocks with a Put Option," is amended as follows:

a. The third through fifth paragraphs of the STATUS section:

~~Statement 125 was issued in June 1996 and was replaced by Statement 140. Statement 140 is effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after March 31, 2001.~~

~~Under Statement 125, the existence of a put option or the probability that it will be exercised did not affect the determination of whether a transfer qualifies for sale treatment. Statement 140 reconsidered this matter and~~ Statement 140 partially nullifies this consensus. Under Statement 140, sale accounting is precluded if a transferor maintains effective control over the transferred financial assets. Statement 166, which was issued in June 2009, amends Statement 140. Paragraph 9(c) of Statement 140 and the related implementation guidance in paragraphs 46A–54A, as amended by Statement 166, provide examples of when a transferor maintains effective control over transferred financial assets.~~the existence of a put option or the probability that it will be exercised *may* affect the determination of whether a transfer qualifies for sale treatment but only if the marketable security is considered a financial asset that is not readily obtainable. For example, put options written to the transferee generally do not constrain it, but a put option on a not-readily-obtainable asset may benefit the transferor and effectively constrain the transferee if the option is sufficiently deep in the money when it is written that it is probable that the transferee will exercise it and the transferor will reacquire the transferred asset.~~

~~Statement 125,~~Statements 140 and 166 do~~es~~ not address subsequent measurement of put options entered into in a transaction accounted for as a sale. The measurement guidance in Issue 85-25 would be retained for transactions accounted for as secured borrowings.

C10. EITF Issue No. 85-40, "Comprehensive Review of Sales of Marketable Securities with Put Arrangements," is amended as follows:

a. The second through eighth paragraphs of the STATUS section:

Statement 125 was issued in June 1996 and was replaced by Statement 140. Statement 140 provides accounting and reporting standards for transfers and servicing of financial assets and extinguishments of liabilities. Statement 166, which was issued in June 2009, amends Statement 140.~~is effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after March 31, 2001. The effective dates for securitization disclosures and accounting for collateral are detailed in paragraphs 22 and 23 of Statement 140.~~

Issue 1a—Statement 140, as amended by Statement 166, ~~partially~~ nullifies this consensus. Under Statement 140, as amended by Statement 166, sale accounting is precluded if a transferor maintains effective control over the transferred financial assets. Paragraph 9(c) of Statement 140 and the related implementation guidance in paragraphs 46A–54A, as amended by Statement 166, provide examples of when a transferor maintains effective control over transferred financial assets.~~the existence of a put option or the probability that it will be exercised *may* affect the determination of whether a transfer qualifies for sale treatment but only if the marketable security is not readily obtainable. For example, put options written to the transferee generally do not constrain it, but a put option on a not-readily-obtainable asset may benefit the~~

~~transferor and effectively constrain the transferee if the option is sufficiently deep in the money when it is written that it is probable that the transferee will exercise it and the transferor will reacquire the transferred asset.~~

Issue 1b—Statement 125 partially nullified this consensus. Statements 140 and 166 do ~~did~~ not reconsider this matter. ~~Neither~~ Statements 125, ~~nor Statement~~ 140, and 166 do not address subsequent measurement of put options entered into in a transaction accounted for as a sale. The measurement guidance in this consensus would be retained for transactions accounted for as secured borrowings.

Issue 2—Statement 140, as amended by Statement 166, ~~partially~~ nullifies this consensus. Under Statement 140, as amended by Statement 166, sale accounting is precluded if a transferor maintains effective control over the transferred financial assets. Paragraph 9(c) of Statement 140 and the related implementation guidance in paragraphs 46A–54A, as amended by Statement 166, provide examples of when a transferor maintains effective control over transferred financial assets. ~~the existence of a put option or the probability that it will be exercised *may* affect the determination of whether the transfer qualifies for sale treatment but only if the marketable security is considered a financial asset that is not readily obtainable. For example, put options written to the transferee generally do not constrain it, but a put option on a not-readily-obtainable asset may benefit the transferor and effectively constrain the transferee if the option is sufficiently deep in the money when it is written that it is probable that the transferee will exercise it and the transferor will reacquire the transferred asset.~~ Statement 140 nullified the Task Force consensus that continual reassessment of the probability that the put option will be exercised is required. Under Statement 140, the assessment of the probability that the put option will be exercised and the transferee constrained is required only at the transaction date. Statement 166 does not amend Statement 140's requirement that such assessment is required only at the transaction date.

Issue 3—Statement 125 partially nullified this consensus. Statements 140 and 166 do ~~did~~ not reconsider this matter. ~~Neither~~ Statements 125, ~~nor Statement~~ 140, and 166 do not address subsequent measurement of put options entered into in a transaction accounted for as a sale. If the security were subsequently repurchased, it would be recorded in accordance with Statement 115.

Issue 4—Statement 125 nullified this consensus. Under Statement 125, the remaining life of a put option did not affect the determination of whether the transfer qualifies for sale treatment. Statements 140 and 166 did not reconsider this matter. ~~Under both Statements 125 and 140, the remaining life of a put option does not affect the determination of whether the transfer qualifies for sale treatment.~~

Issue 5—Statement 125 nullified this consensus. ~~Statement 140 did not reconsider this matter.~~ Statement 125 call~~s~~ed for recognition of liabilities (including put options) incurred in consideration as proceeds of the sale of a financial asset and initial measurement at fair value, if practicable. ~~If it is not practicable to measure the fair value of a liability incurred in a sale, then the transferor will recognize no gain.~~ Statement 140 did not reconsider this matter. Statement 166, which amends Statement 140, removes the practicability exception for the requirement to initially measure proceeds of a sale at fair value.

C11. EITF Issue No. 87-18, "Use of Zero Coupon Bonds in a Troubled Debt Restructuring," is amended as follows:

a. The fourth and fifth paragraphs of the STATUS section:

   This Issue was partially resolved by Statement 125, which was issued in June 1996. Statement 125 was replaced by Statement 140. Statement 166, which was issued in June 2009, amends Statement 140. ~~Neither~~ Statements 125, ~~nor Statement~~ 140, and 166 do not affect the consensus regarding loss recognition. However, if the creditor has the right to sell or pledge the collateral:

   1. Paragraph 15 of Statement 140 requires that the debtor reclassify the collateral and report it in its statement of financial position separately from other assets not so encumbered. Statement 166 does not reconsider this matter.
   2. Paragraph 17 of Statement 140, as amended by Statement 166, requires the creditor to disclose the fair value of that collateral and of the portion that it has sold or repledged.

   If the creditor does not have the right to sell or pledge the collateral, paragraph 17 of Statement 140, as amended by Statement 166, requires that the debtor disclose ~~the carrying amount and classification of the~~ information about that collateral.

C12. EITF Issue No. 87-30, "Sale of a Short-Term Loan Made under a Long-Term Credit Commitment," is amended as follows:

a. The first through fifth paragraphs of the STATUS section:

   Statement 125, which superseded Statement 77, was issued in June 1996. Statement 125 was replaced by Statement 140 in September 2000. Statement 140 affirmed the Task Force consensus on the principal issue, nullified a matter noted by the Task Force Chairman, partially resolved a matter noted by the SEC Observer, and had no effect on the remaining issues in this Issue. Statement 166, which was issued in June 2009, amends Statement 140.

   A transfer of a short-term loan under a long-term credit commitment to a third-party purchaser without recourse could meet the conditions for surrendering control under paragraph 9 of Statement 140, as amended by Statement 166. The specific circumstances in transactions taking place in practice have to be judged in light of the ~~criteria~~ conditions specified in paragraph 9 of Statement 140, as amended by Statement 166.

   To the extent that the transaction described in Issue 87-30 is accounted for as the transfer of a receivable with a put option, Statement 140 ~~would~~ requires sale treatment if the conditions of paragraph 9 of Statement 140, as amended by Statement 166, are met. ~~However, the existence of a put option or the probability that it will be exercised *may* affect the determination of whether the transfer qualifies as a sale.~~

   ~~For example, a put option written to the transferee for a not-readily-obtainable asset may benefit the transferor and effectively constrain the transferee from selling or repledging the asset, thereby precluding sale accounting, if it is probable at the date of transfer (because the option is sufficiently deep in the money when the option is written) that the transferee will exercise the put option and the transferor will reacquire the transferred asset. As a result,~~ Statement 140 ~~nullifies~~ nullified ~~this~~ the matter noted by the Task Force Chairman.

   Statement 166 does not reconsider this matter, but it amends the guidance in paragraph 9 of Statement 140. Under Statement 140, as amended by Statement 166, sale accounting is precluded if a transferor maintains effective control over the transferred financial assets. Paragraph 9(c) of Statement 140 and the related implementation guidance in paragraphs 46A–54A, as amended by Statement 166, provide examples of when a transferor maintains effective control over transferred financial assets.

C13. EITF Issue No. 88-20, "Difference between Initial Investment and Principal Amount of Loans in a Purchased Credit Card Portfolio," is amended as follows:

a. The third paragraph of the STATUS section:

   Statement 125 was issued in June 1996. Statement 125 was replaced by Statement 140 in September 2000, without reconsideration of this matter. Under both Statements 125 and 140, if the transaction described in Issue 1 of Issue 88-20 meets the ~~criteria~~ conditions for sale treatment in paragraph 9, the transferee would recognize all assets obtained and liabilities incurred and initially measure them at fair value. Issue 2 concerning the periods over which the amounts allocated to the loans acquired and the identifiable asset should be amortized, is outside of the scope of both Statements 125 and 140 because they do not address subsequent measurement of such items. Statement 166, which was issued in June 2009, amends Statement 140 without reconsideration of these matters. However, Statement 166 amends the guidance in paragraph 9 of Statement 140.

C14. EITF Issue No. 88-22, "Securitization of Credit Card and Other Receivable Portfolios," is amended as follows:

a. The second and fourth through seventh paragraphs of the STATUS section:

~~A related issue was discussed in Issue No. 88-11, "Allocation of Recorded Investment When a Loan or Part of a Loan Is Sold." That Issue considers how an enterprise's recorded investment in a loan should be allocated between the portion of the loan sold (for purposes of determining the gain or loss on the sale) and the portions that continue to be held by a transferor (for purposes of determining the remaining recorded investment).~~

Statement 125 was issued in June 1996. Statement 125 was replaced by Statement 140 in September 2000. Statement 140 nullified the consensuses in Issues 1 and 2 and affirmed the consensus in Issue 3. Statement 166, which was issued in June 2009, amends Statement 140. Statement 140, as amended by Statement 166, does not reconsider these Issues.

~~Issue 1—On the first issue, Statement 140 carries forward the supersession of Statement 77 and requires sale treatment if, and only if, the transferor has surrendered control in accordance with paragraph 9. Assuming that the criteria in paragraph 9 are met, the transfer would be accounted for as a sale and the bank would:~~

~~1. Recognize and measure a servicing asset in accordance with paragraphs 58-63 of Statement 140~~
~~2. Continue to carry its interests that continue to be held by the transferor in the assets transferred to the SPE~~
~~3. Allocate the previous carrying amount of the credit card and other receivables transferred to the SPE between assets sold and interests that continue to be held by the transferor based on their relative fair value at the date of transfer~~
~~4. Recognize an asset or liability for the forward commitment to transfer future receivables.~~

~~As a result, the consensus on the first issue is nullified by Statement 140.~~

~~Issue 2—Under Statement 140, the method of trust liquidation would not affect the determination of whether the transferor would receive sale treatment under paragraph 9 or secured borrowing treatment under paragraphs 12 and 15. Liquidation methods may allocate receipts of principal or interest between investors and transferors in different proportions than their stated percentage of ownership interests. Those agreed-upon allocations should be taken into consideration in determining the relative fair values of the portion of trust assets beneficially owned by the investors and the seller, which is the basis for allocating the previous carrying amount between the portion of receivables sold to investors and the interests that continue to be held by the transferor. The right to the portion of receivables that will remain in the trust after investors have been completely paid off is part of the interests that continue to be held by the transferor at the outset and hence, was never sold to investors. As a result, the second issue is nullified by Statement 140.~~

~~Issue 3—Under paragraph 75 of Statement 140, any gain or loss recognition for revolving-period receivables sold to a~~

~~securitization trust is limited to receivables that exist and have been sold. As a result, Statement 140 affirms the consensus in the third issue.~~

~~In addition,~~ Statement 140 ~~it~~ affirms the Task Force members' notes that:~~1. The~~ the terms of a transaction should be recognized for the costs expected to be incurred for all future servicing obligations, including costs for receivables not yet sold. Statement 140 requires that a servicer recognize a servicing liability if the benefits of servicing are not expected to adequately compensate the servicer for performing the services, which may well be the case if the work was expected to be performed at a loss. *Adequate compensation* is defined in paragraph 364 of Statement 140. ~~2. Transaction~~ Task Force members also noted that transaction costs relating to the sale of the receivables may be recognized over the initial and reinvestment periods in a rational and systematic manner unless the transaction results in a loss.

According to Statement 140, transaction costs for a past sale are not an asset and thus are part of the gain or loss on sale. In a credit card securitization, however, some of the transaction costs incurred at the outset relate to the future sales that are to occur during the revolving period, and thus can qualify as an asset. Therefore, the observations of Task Force members relating to transaction costs is consistent with Statement 140.

Statement 166 does not reconsider Task Force members' notes.

C15. EITF Issue No. 96-10, "Impact of Certain Transactions on the Held-to-Maturity Classification under FASB Statement No. 115," is amended as follows:

a. The first paragraph of the STATUS section:

Statement 125 was issued in June 1996 and partially nullified this Issue. Statement 125 was replaced by Statement 140 in September 2000, without reconsideration of this matter. Statement 166, which was issued in June 2009, amends Statement 140 without reconsideration of this matter. Paragraph 9 of Statement 140, as amended by Statement 166, contains the requirements for transfers of financial assets to be accounted for as sales. Paragraph 99 of Statement 140 contains additional guidance for wash sales. That paragraph states that wash sales that previously were not recognized if the same financial asset was purchased soon before or after the date shall be accounted for as sales. Unless there is a concurrent contract to repurchase or redeem the transferred financial assets from the transferee, the transferor does not maintain effective control over the transferred financial assets. Thus, wash sale and bond swap agreements in which the transferor does not maintain effective control are required to be accounted for as sales.

C16. EITF Issue No. 96-19, "Debtor's Accounting for a Modification or Exchange of Debt Instruments," is amended as follows:

a. The first paragraph of the STATUS section:

Statement 140 was issued in September 2000 and superseded Statement 125. Statement 140 does not change the guidance dealing with accounting for extinguishments of liabilities. Statement 166, which was issued in June 2009, amends Statement 140 without reconsideration of this matter.

C17. EITF Issue No. 97-3, "Accounting for Fees and Costs Associated with Loan Syndications and Loan Participations after the Issuance of FASB Statement No. 125," is amended as follows:

a. The first paragraph of the STATUS section:

Statement 140 was issued in September 2000 and replaced Statement 125. Statement 140 does not affect the Task Force consensuses in this Issue. Statement 166, which was issued in June 2009, amends Statement 140 without reconsideration of this matter.

C18. EITF Issue No. 98-8, "Accounting for Transfers of Investments That Are in Substance Real Estate," is amended as follows:

a. Paragraph 8:

> Statement 140 was issued in September 2000. ~~It is effective for transfers of financial assets occurring after March 31, 2001.~~ Paragraph 4 of Statement 140 provides that transfers of ownership interests that are in substance the sale of real estate are outside the scope of Statement 140. Therefore, these transfers should follow the guidance in Statement 66. As a result, this Issue is affirmed by the issuance of Statement 140. Statement 166, which was issued in June 2009, amends Statement 140 without reconsideration of this matter.

C19. EITF Issue No. 98-14, "Debtor's Accounting for Changes in Line-of-Credit or Revolving-Debt Arrangements," is amended as follows:

a. Paragraph 7:

> Statement 140 was issued in September 2000 and superseded Statement 125. Statement 140 does not change the guidance dealing with accounting for modifications of debt or extinguishments of liabilities. Statement 166, which was issued in June 2009, amends Statement 140 without reconsideration of this matter.

C20. EITF Issue No. 98-15, "Structured Notes Acquired for a Specified Investment Strategy," is amended as follows:

a. Paragraph 7:

> Statement 140 was issued in September 2000 and replaced Statement 125. Statement 140 does not affect the Task Force consensus in this Issue. However, Statement 166, which was issued in June 2009, amends Statement 140's requirements for accounting for transfers that satisfy the conditions to be accounted for as sales. Under Statement 140, as amended by Statement 166, the guidance in paragraph 11 of that Statement should be applied to each structured note upon transfer.

C21. EITF Issue No. 99-8, "Accounting for Transfers of Assets That Are Derivative Instruments but That Are Not Financial Assets," is amended as follows:

a. Paragraph 5:

> Statement 140, which replaced Statement 125, was issued in September 2000, without reconsideration of this matter. Statement 166, which was issued in June 2009, amends Statement 140 without reconsideration of this matter.

C22. EITF Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests That Continue to Be Held by a Transferor in Securitized Financial Assets," is amended as follows:

a. Title:

> Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Transferor's Beneficial Interests ~~That Continue to Be Held by a Transferor~~ in Securitized Financial Assets Obtained in a Transfer Accounted for as a Sale

b. Footnote 1 to paragraph 1:

> Paragraph 364 of Statement 140, as amended by Statement 166, defines beneficial interests as "rights to receive all or portions of specified cash inflows ~~to~~ received by a trust or other entity, including, but not limited to, senior and subordinated shares of interest, principal or other cash inflows to be 'passed-through' or 'paid-through,' premiums due to guarantors, commercial paper obligations, and residual interests, whether in the form of debt or equity."

c. Paragraph 5:

> The scope of this Issue includes a transferor's beneficial interests obtained as proceeds ~~that continue to be held by a transferor~~ in securitization transactions that are accounted for as sales under Statement 140, as amended by Statement 166, [Note: See paragraph 20 of the STATUS section.] and purchased beneficial interests in securitized financial assets. The scope includes beneficial interests that:
>
> a. Are either debt securities under Statement 115 or required to be accounted for like debt securities under Statement 115 pursuant to paragraph 14 of Statement 140, as amended by Statement 166.

b. Involve securitized financial assets that have contractual cash flows (for example, loans, receivables, debt securities, and guaranteed lease residuals, among other items). Thus, the consensus in this Issue does not apply to securitized financial assets that do not involve contractual cash flows (for example, common stock equity securities, among other items). The Task Force observed that the guidance in Issue No. 96-12, "Recognition of Interest Income and Balance Sheet Classification of Structured Notes," may be applied to those beneficial interests involving securitized financial assets that do not involve contractual cash flows.
c. Do not result in consolidation of the entity issuing the beneficial interests by the holder of the beneficial interests. [Note: See STATUS section.]
d. Are not within the scope of Practice Bulletin 6 (as amended by Statements 114 and 115 and SOP 03-3) or SOP 03-3. [Note: See paragraph 10 of this Issue.]
e. Are not beneficial interests in securitized financial assets that (1) are of high credit quality (for example, guaranteed by the U.S. government, its agencies, or other creditworthy guarantors, and loans or securities sufficiently collateralized to ensure that the possibility of credit loss is remote) and (2) cannot contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment. Instead, interest income on such beneficial interests should be recognized in accordance with the provisions of Statement 91, and determining whether an other-than-temporary impairment of such beneficial interests exists should be based on FSP EITF 99-20-1, FSP FAS 115-1 and FAS ~~/~~124-1, Statement 115, SAB 59, SAS 92, and the Statement 115 Special Report.

d. Paragraph 11:

The Task Force reached a consensus that the holder should recognize the excess of all cash flows attributable to the beneficial interest estimated at the acquisition/transaction date (referred to herein as the transaction date) over the initial investment (the accretable yield) as interest income over the life of the beneficial interest using the effective yield method. If the holder of the beneficial interest is the transferor, the initial investment would be ~~the allocated carrying amount after application of the relative~~ the fair value of the beneficial interest as of the date of transfer, as ~~allocation method~~ required by Statement 140, as amended by Statement 166. [Note: See paragraph 20 of the STATUS section.] The amount of accretable yield should not be displayed in the balance sheet.

e. Paragraph 14:

~~Consistent with the guidance in Topic No. D-75, "When to Recognize Gains and Losses on Assets Transferred to a Qualifying Special-Purpose Entity," and the guidance provided by the FASB staff in its answers to questions 59–63 of the Statement 140 Special Report, the application of this consensus to securities accounted for as available-for-sale by the transferor prior to the transfer should not result in recognition of an unrealized gain or loss as interest income before the gain or loss on those securities is realized. [Note: See paragraph 20 of the STATUS section.] That is, under this consensus, an entity should retain the available-for-sale classification of the interest that continues to be held by a transferor and should not recognize, as interest income over the life of that interest that continues to be held by a transferor, the unrealized gain or loss that was recorded in other comprehensive income prior to the transfer unless a portion of the unrealized gain or loss recorded in other comprehensive income must be included in income as a component of the recognition of an other-than-temporary impairment. This guidance would only apply to the extent of the interest that continues to be held by a transferor, not the interest considered sold under Statement 140.~~

f. Paragraph 16:

~~The Task Force also reached a consensus that in situations in which it is not practicable for a transferor to estimate the fair value of the beneficial interest at the initial transfer date, interest income should not be recognized using the interest method. For these beneficial interests (that is, those beneficial interests that continue to be held by a transferor that are recorded at $0 pursuant to Statement 140), the transferor should use the cash basis for recognizing interest income because the beneficial interest will have an allocated carrying amount of zero.~~

g. Paragraphs 20 and 21:

20. Statement 140 replaced Statement 125 in September 2000. ~~Statement 140 nullified Topic D-75 because the activities described in that Topic are no longer appropriate for qualifying special-purpose entities. However, Statement 140 carried over from Statement 125 without reconsideration the standards that underlay the guidance in Topic D-75: a sale can be recognized only to the extent that consideration other than beneficial interests in the transferred asset is received in exchange, and a sale and the resulting gain or loss is to be recognized upon completion of a transfer of assets that satisfies the conditions to be accounted for as a sale.~~ Statement 166, which was issued in June 2009, amends Statement 140. This Issue has been revised to reflect the Board's decisions in Statement 166, which removes the concept of a qualifying special-purpose entity and removes the scope exception for a qualifying special-purpose entity from Interpretation 46(R). Statement 140, as amended by Statement 166, requires that derecognition provisions be applied to a transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset. (The example in Exhibit 99-20B involving a partial sale of a financial asset and a qualifying special-purpose entity has been removed.) Statement 140, as amended by Statement 166, requires that interests obtained by a transferor upon completion of a transfer of an entire financial asset or a group of entire financial assets that satisfies the conditions to be accounted for as a sale be recognized and initially measured at fair value. Statement 166 removes the practicability exception for the requirement to initially measure assets obtained and liabilities incurred as proceeds of a sale at fair value. Statement 140, as amended by Statement 166, applies the term *interests that continue to be held by a transferor* only to participating interests (the term *participating interest* is defined in paragraph 8B of Statement 140, as added by Statement 166) retained by the transferor upon completion of a transfer of participating interests that satisfies the conditions for sale accounting. This Issue reflects the Board's decision in Statement 166 to limit the use of the term *interests that continue to be held by the transferor* only to those retained participating interests. (Paragraphs in this Issue affected by the issuance of Statement 166 solely due to this change in terminology have been excluded from this Issue.)

[Paragraph 21 includes amendments that also are included in FASB Statement No. 167, *Amendments to FASB Interpretation No. 46(R)*.]

21. ~~Interpretation 46 and~~ Interpretation 46(R), as amended by Statement 167, addresses consolidation by business enterprises of variable interest entities, which include many special-purpose entities used in securitization transactions~~ if they are not qualifying special-purpose entities~~. ~~Interpretation 46 and~~ That Interpretation ~~46(R)~~ requires a variable interest entity to be consolidated by an enterprise if that enterprise has a variable interest (or a combination of variable interests) that provides the enterprise with a controlling financial interest. Paragraphs 14–14G of Interpretation 46(R), as amended by Statement 167, provide guidance on determining whether an enterprise has a controlling financial interest in a variable interest entity.~~will absorb a majority of the entity's expected losses or is entitled to receive a majority of the entity's expected residual returns or both.~~

h. Paragraph 27:

Statement 156, issued in March 2006, amends Statement 140 with respect to the accounting for separately recognized servicing assets and servicing liabilities. Statement 156 does not affect any of the consensuses reached in this Issue.~~; however, this Issue reflects the Board's decision in Statement 156 to replace the term *retained interests* with *interests that continue to be held by a transferor.*~~

i. Exhibit 99-20B is deleted because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity.

C23. EITF Issue No. 02-9, "Accounting for Changes That Result in a Transferor Regaining Control of Financial Assets Sold," is amended as follows:

a. Paragraph 1:

A key concept in Statement 140 is that a transferred financial asset that has been accounted for as sold is accounted for as "re-purchased" if the basis for that sale accounting becomes invalid subsequent to the initial accounting for the transaction. That concept is articulated in paragraphs 55 and 55A of Statement 140, as amended by Statement 166, which states:

> 55. A change in law~~, status of the transferee as a qualifying SPE,~~ or other circumstance may result in a transferred portion of an entire financial asset no longer meeting the conditions of a participating interest (paragraph 8B) or the transferor's regaining control of transferred financial assets after a transfer that was previously accounted for ~~appropriately~~ as a sale~~having been sold~~, because one or more of the conditions in paragraph 9 are no longer met. Such changes~~a change~~, unless ~~it arises~~ they arise solely from ~~either~~ the initial application of this Statement, from consolidation of an entity involved in the transfer at a subsequent date (paragraph 55A), or from a change in market prices (for example, an increase in price that moves into-the-money a freestanding call on a non-readily-obtainable transferred financial asset that was originally sufficiently out-of-the-money that it was judged not to constrain the transferee), are ~~is~~ accounted for in the same manner as a purchase of the transferred financial assets from the former transferee(s) in exchange for liabilities assumed (paragraph 10 or 11). After that change, the transferor recognizes in its financial statements those transferred financial assets together with liabilities to the former transferee(s) or ~~BIHs in those assets (paragraph 38)~~beneficial interest holders of the former transferee(s). The transferor initially measures those transferred financial assets and liabilities at fair value on the date of the change, as if the transferor purchased the transferred financial assets and assumed the liabilities on that date. The former transferee would derecognize the transferred financial assets on that date, as if it had sold the transferred financial assets in exchange for a receivable from the transferor.
>
> 55A. If a transferor subsequently consolidates an entity involved in a transfer that was accounted for as a sale, it shall account for the consolidation in accordance with applicable consolidation accounting guidance.

One ~~Two~~ circumstance~~s~~ that has ~~have~~ raised questions about the application of paragraph 55 occurs when the provisions of paragraph 55 are triggered because ~~(a) a qualifying special-purpose entity (SPE) becomes nonqualifying and (b)~~ the transferor holds a contingent right such as a contingent call option on the transferred financial assets (for example, a removal of accounts provision or "ROAP") and the contingency has been met. This Issue assumes that the transferee is not consolidated by the transferor.

b. Paragraph 2:

~~A qualifying SPE may become nonqualifying or "tainted" for several reasons, including a decision by the outside beneficial interest holders to grant the SPE decision-making powers that are prohibited for qualifying SPEs. Under the requirements of paragraph 55, the disqualification of a formerly qualifying SPE will generally result in the "re-purchase" by the transferor of *all* assets sold to and still held by the SPE because the transferee (the SPE that is no longer qualifying) is constrained from pledging or exchanging the financial assets and this condition provides more than a trivial benefit to the transferor (refer to paragraph 9(b) of Statement 140). This Issue considers the application of the guidance in paragraph 55 prior to any consideration of whether the transferee (for example, an SPE) should be consolidated and, therefore, prior to considering any eliminating entries that may result from consolidation.~~

c. Paragraph 3:

Under Statement 140, rights held by the transferor (typically in the form of purchased options or forward purchase contracts) preclude sale accounting under paragraph 9(c)~~(2)~~ if they provide the transferor with (a) the *unilateral* right to cause the holder to return *specific* transferred financial assets and (b) more than a trivial benefit. One class of contingent rights (including certain ROAPs[1]) does not preclude sale accounting because it does not include unilateral rights. The most common type of ROAP is a default ROAP, which gives the holder the right but not the obligation to purchase (call) a loan that is in default (the meaning of default typically is specifically defined in each transaction). Such rights are common in credit card securitizations and in securitizations sponsored by the Government National Mortgage Association (GNMA)[2] and other governmental or quasi-governmental agencies. Once the contingency is met (in this case, when a given loan goes into default), the call option on that asset (loan) is no longer contingent. At that point, the transfer fails the criterion in paragraph 9(c)~~(2)~~ of Statement 140 because the transferor has the unilateral right to purchase a specific transferred financial asset and obtains more than a trivial benefit from that right. Under the requirements of paragraph 55, when a contingency related to a transferor's contingent right has been met, the transferor generally must account for the "re-purchase" of a *specific subset* of the financial assets transferred to and held by the ~~qualifying SPE~~entity. The transferor must do so *regardless of whether it intends to exercise its call option.*

d. Paragraph 4:

[For ease of use, only the issues in the paragraph affected by this Statement have been reproduced.]

Issue 1—How the transferor should account for the transferor's beneficial interests ~~that continue to be held by the transferor~~ when the underlying assets are re-recognized under the provisions of paragraph 55 because the transferor's contingent right (for example, a ROAP or other contingent call option on the transferred financial assets) becomes exercisable, including whether any gain or loss should be recognized by the transferor when paragraph 55 is applied.

~~Issue 2—How assets re-recognized by the transferor that were previously sold to an SPE that was formerly considered qualifying should be accounted for when the entire SPE becomes non-qualifying under the provisions of paragraph 55, including whether any gain or loss should be recognized by the transferor when paragraph 55 is applied~~

Issue 5—After a paragraph 55 event, how the transferor should account for the transferor's interests ~~that continue to be held by the transferor~~ (other than the servicing asset).

e. Paragraph 5:

The Task Force reached a consensus on Issue 1 that upon application of paragraph 55, no gain or loss should be recognized in earnings with respect to any of the transferor's beneficial interests ~~that continue to be held by the transferor~~. Beneficial interests should be evaluated periodically for possible impairment, including at the time paragraph 55 is applied. A gain or loss may be recognized upon the exercise of a ROAP or similar contingent right with respect to the "re-purchased" ~~portion of the~~ transferred financial assets that were sold if the ROAP or similar contingent right held by the transferor is not accounted for as a derivative under Statement 133 and is not at-the-money, resulting in the fair value of those repurchased financial assets being greater or less than the related obligation to the transferee.

f. Paragraph 6:

~~The Task Force reached a consensus on Issue 2 that in the event the entire SPE becomes nonqualifying upon application of paragraph 55, no gain or loss should be recognized with respect to the "re-purchase" by the transferor of the financial assets originally sold that remain outstanding in the SPE (or the portion thereof if the transferor continues to hold an interest in those assets). The fair value of the re-recognized assets will equal the fair value of the liability assumed by the transferor because the transferor is contractually required to pass on 100 percent of the cash flows from the re-recognized assets to the SPE for distribution in accordance with the contractual documents governing the SPE. The process of determining the fair value of both the re-recognized assets and the assumed liability may require a careful analysis of all of the expected cash flows of the securitization vehicle, including cash flows of assets within the vehicle that are not subject to paragraph 55 (for example, proceeds that are temporarily reinvested by the SPE). In performing that analysis, the transferor would need to consider both the timing and the amounts of the expected cash flows and also which party has rights to such expected cash flows at the time of the paragraph 55 event.~~

g. Paragraph 9:

The Task Force reached a consensus on Issue 5 that when a paragraph 55 event occurs, the transferor should continue to account for the transferor's interests ~~that continue to be held by the transferor~~ in those underlying financial assets apart from any re-recognized financial assets. That is, the transferor's interests ~~that continue to be held by the transferor~~ should not be combined with and accounted for with the re-recognized financial assets. However, a subsequent event that results in the transferor reclaiming those financial assets from the transferee—for example, the exercise of a ROAP or the consolidation by the transferor of the ~~SPE~~ securitization entity in accordance with applicable generally accepted accounting principles, including Interpretation 46(R)—would result in a recombination of the transferor's interests ~~that continue to be held by the transferor~~ with the underlying financial assets.

h. Paragraph 13:

Statement 156, issued in March 2006, amends Statement 140 with respect to the accounting for separately recognized servicing assets and servicing liabilities. Statement 156 does not affect any of the consensuses reached in this Issue~~; however, this Issue reflects the Board's decision in Statement 156 to replace the term *retained interests* with *interests that continue to be held by a transferor*~~. The application section of this Issue has been revised to initially measure separately recognized servicing assets at fair value.

i. Paragraph 13A is added as follows:

Statement 166, which was issued in June 2009, amends Statement 140. This Issue has been revised to reflect the amendments in Statement 166. The examples of the application of the consensuses in this Issue also have been revised to reflect the amendments in Statement 166.

j. Exhibit 02-9A and its related footnote 14:

EXAMPLES OF THE APPLICATION OF THE EITF CONSENSUSES ON ISSUE 02-9

[Examples 1–3, including footnotes 3–13, are deleted because Statement 140, as amended by Statement 166, removes the concept of a qualifying special-purpose entity. For ease of use, they have not been reproduced here.]

Issues 4 and 5—Accounting for Servicing Asset and Subsequent Accounting for Transferor's Interest ~~That Continues to Be Held by Transferor~~

Example 4—Transferor's Interest ~~That Continues to Be Held by Transferor~~ Accounted for as an Available-for-Sale Security with a Servicing Asset

This example assumes the following facts:

On January 2, 20X1, Company A originates $1,000 of loans, yielding 10.5 percent interest income for their estimated life of 9 years. Company A later transfers the loans in their entirety to an unconsolidated entity and accounts for the transfer as a sale. Company A receives as proceeds ~~sells, through a "two-step" transfer using a qualifying SPE, the~~ $1,000 cash plus a beneficial interest that entitles it ~~principal plus the right~~ to receive ~~interest income of 8~~ 1 percent of the contractual interest (an interest-only strip receivable)~~to investors for $1,000~~. Company A will continue to service the loans for a fee of 100 basis points. ~~Company A retains a 100 basis point interest-only (IO) strip receivable.~~ The guarantor, a third party, receives 50 basis points as a guarantee fee.

At the date of transfer:

- The fair value of the servicing asset is $40.
- The total fair value of the loans including servicing is $1,040 ~~(allocated cost is $945.50)~~.
- The fair value of the interest-income strip receivable is $60 ~~(allocated cost is $54.50)~~.

On December 1, 20X1, an event occurs that results in the transfer not meeting the conditions for sale accounting~~qualifying SPE being disqualified~~. The fair value ~~of the portion~~ of the originally transferred financial assets ~~that were previously accounted for as sold~~ that remain outstanding in the ~~SPE~~ entity on that date is $929. The fair value of the Transferor's interest ~~that continues to be held by Transferor~~ (in the form of an interest-only ~~IO~~ strip) on that date is $58. The fair value of the servicing asset on that date is $38. The guarantee that was entered into by the ~~SPE~~ entity does not trade with the underlying financial assets. The fees on this guarantee will be paid as part of the cash waterfall.[14]

Issue 4—Accounting for Servicing Asset before and after a Paragraph 55 Event

Once a servicing asset is recognized it should not be added back to the underlying financial asset. Even when the transferor has regained control over the underlying financial asset~~s~~ via a paragraph 55 event, the related servicing asset should continue to be separately recognized.

Issue 5—Subsequent Accounting for Transferor's Interests ~~That Continue to Be Held by Transferor~~

Example 5—Accounting for the Sale of Loans When the Transferor's Interest ~~That Continues to Be Held by Transferor~~ Is an Interest-Only ~~IO~~ Strip That Is Accounted for at Fair Value in the Same Manner as an Available-for-Sale Security (per Paragraph 14 of Statement 140)

This example is based on the same facts as those assumed under Example 4. The accounting for the servicing asset after a paragraph 55 event has occurred is discussed in Issue 4.

~~Carrying Amount Based on Relative Fair Values~~

	~~Fair Value~~	~~Percentage of Total Fair Value~~	~~Allocated Carrying Amount~~
~~Loans~~	~~$ 1,040~~	~~94.55~~	~~$ 945.50~~
~~Interest that continues to be held by Transferor~~	~~60~~	~~5.45~~	~~54.50~~
~~Total~~	~~$ 1,100~~	~~100.00~~	~~$ 1,000.00~~

January 2, 20X1

Cash	$ 1,000~~.00~~	
Transferor's ~~I~~interest ~~that continues to be held by Transferor~~ (available for sale)	60~~54.50~~	
Servicing asset	40~~.00~~	
Loans		$ 1,000~~.00~~
Gain on sale		100~~94.50~~

To record the sale of the assets and to recognize Transferor's interest ~~that continues to be held by Transferor~~ and a servicing asset at fair value.

December 1, 20X1

~~Interest that continues to be held by Transferor (available for sale)~~	~~$ 3.50~~	
~~Other comprehensive income~~		~~$ 3.50~~
Other comprehensive income	$ 2	
Transferor's interest (available for sale)		$ 2

To subsequently measure ~~the~~ Transferor's interest ~~that continues to be held by Transferor~~ in the same manner as an available-for-sale security.

After the Paragraph 55 Event

December 1, 20X1

Loans	$ 929	
Due to ~~SPE~~Securitization Entity		$ 929

To recognize the previously sold loans on Transferor's books along with the obligation to pass the cash flows associated with those loans to ~~SPE~~ Securitization Entity.

Accounting for the Re-Recognized Financial Assets and Transferor's Interests ~~That Continue to Be Held by Transferor~~

- Transferor would continue to account for ~~the~~ Transferor's interests ~~that continue to be held by Transferor~~ (in accordance with paragraph 13 of Statement 115) at fair value with changes in fair value recognized in other comprehensive income.
- Transferor would account for the loans at cost plus accrued interest in accordance with Statement 91.

[14]All cash flows from the financial assets transferred to the trust are initially sent directly to the trust and then distributed in order of priority. The priority of payments in the cash waterfall is as follows: servicing fees, guarantees, amounts due to outside beneficial interest holders, and amounts due to ~~the~~ Transferor's beneficial interest ~~that continues to be held by Transferor~~.

C24. EITF Topic No. D-51, "The Applicability of FASB Statement No. 115 to Desecuritizations of Financial Assets," is amended as follows:

a. The first and second paragraphs of the Accounting for Desecuritizations section:

The FASB staff notes that Statement 115 does not address the accounting for desecuritizations but that FASB Statement No. 140~~125~~, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* as amended by FASB Statement No. 166, *Accounting for Transfers of Financial Assets,* does address the accounting for the securitization of financial assets. ~~Paragraph 9 of Statement 125 states:~~

~~A transfer of financial assets (or all or a portion of a financial asset) in which the transferor surrenders control over those financial assets shall be accounted for as a sale *to the extent that consideration other than beneficial interests in the transferred assets is received in exchange*. [Emphasis added.]~~

While Statement 140~~125~~, as amended by Statement 166, does not specifically address the accounting for desecuritization transactions, the FASB staff believes that the guidance in paragraph 9 of that Statement should be extended by analogy to those transactions. ~~Thus, the FASB staff believes that the transfer of securities or beneficial interests in a securitized pool of financial assets in which the transferor receives in exchange only the financial assets underlying those securities or beneficial interests would not be accounted for as a sale.~~

b. The second paragraph of the Subsequent Developments section:

~~Statement 140 is effective for transfers of financial assets occurring after March 31, 2001. The provisions of paragraph 9 of Statement 125 cited in this announcement were carried forward without reconsideration. As a result, t~~The guidance in this announcement was unaffected by the issuance of Statement 140. However, Statement 166, which was issued in June 2009, amends the requirements in paragraph 9 of Statement 140. The guidance in this announcement has been revised to reflect the effects of Statement 166. Statement 166 does not affect the guidance in this announcement on accounting for desecuritizations of financial assets classified as held to maturity.

C25. EITF Topic No. D-65, "Maintaining Collateral in Repurchase Agreements and Similar Transactions under FASB Statement No. 125," is amended as follows:

a. The first paragraph of the Subsequent Developments section:

> Statement 125 was replaced by FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* in September 2000. Statement 125's provisions on maintenance of collateral in repurchase agreements and similar transactions were carried forward without reconsideration of this matter. FASB Statement No. 166, *Accounting for Transfers of Financial Assets,* which was issued in June 2009, amends Statement 140 without reconsideration of this matter.

Appendix D

STATEMENT 140 MARKED TO SHOW CHANGES MADE BY THIS STATEMENT

D1. This Statement amends FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. This appendix contains the following sections of Statement 140, as amended, marked to show changes from this Statement: Introduction and Scope, Standards of Financial Accounting and Reporting, Appendix A: Implementation Guidance, Appendix C: Illustrative Guidance, and Appendix E: Glossary. This appendix does not contain a separate summary or the appendixes for Background Information and Basis for Conclusions or Amendments to Existing Pronouncements. [Added text is underlined and deleted text is ~~struck out~~.]

INTRODUCTION AND SCOPE

1. The Board added a project on financial instruments and off-balance-sheet financing to its agenda in May 1986. The project is intended to develop standards to aid in resolving existing financial accounting and reporting issues and other issues likely to arise in the future about various financial instruments and related transactions. The November 1991 FASB Discussion Memorandum, *Recognition and Measurement of Financial Instruments,* describes the issues to be considered. This Statement focuses on the issues of accounting for **transfers**[1] and servicing of **financial assets** and extinguishments of liabilities.

2. Transfers of financial assets take many forms. Accounting for transfers in which the **transferor** has no **continuing involvement** with the transferred financial assets or with the **transferee** has not been controversial. However, transfers of financial assets often occur in which the transferor has some continuing involvement either with the assets transferred or with the transferee. Examples of continuing involvement with the transferred financial assets include, but are not limited to, servicing arrangements, **recourse**~~,~~ ~~servicing,~~ or guarantee arrangements, agreements to ~~reacquire~~ purchase or redeem transferred financial assets, options written or held, **derivative financial instruments** that are entered into contemporaneously with, or in contemplation of, the transfer, arrangements to provide financial support, ~~and~~ pledges of **collateral,** and the transferor's **beneficial interests** in the transferred financial assets. Transfers of financial assets with continuing involvement raise issues about the circumstances under which the transfers should be considered as sales of all or part of the assets or as secured borrowings and about how transferors and transferees should account for sales and secured borrowings. This Statement establishes standards for resolving those issues.

3. An entity may settle a liability by transferring assets to the creditor or otherwise obtaining an unconditional release. Alternatively, an entity may enter into other arrangements designed to set aside assets dedicated to eventually settling a liability. Accounting for those arrangements has raised issues about when a liability should be considered extinguished. This Statement establishes standards for resolving those issues.

4. This Statement does not address transfers of custody of financial assets for safekeeping, contributions,[2] transfers of ownership interests that are in substance sales of real estate, or investments by owners or distributions to owners of a business enterprise.

[1]Terms defined in Appendix E, the glossary, are set in **boldface type** the first time they appear.

[2]Contributions—unconditional nonreciprocal transfers of assets—are addressed in FASB Statement No. 116, *Accounting for Contributions Received and Contributions Made.*

This Statement does not address subsequent measurement of assets and liabilities, except for (a) **servicing assets** and **servicing liabilities** and (b) **interest-only strips,** ~~securities,~~ other beneficial interests ~~that continue to be held by a transferor in securitizations~~, loans, other receivables, or other financial assets that can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment and that are not within the scope of FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities.* This Statement does not change the accounting for employee benefits subject to the provisions of FASB Statement No. 87, *Employers' Accounting for Pensions,* No. 88, *Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits,* or No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions.* This Statement does not change the provisions relating to leveraged leases in FASB Statement No. 13, *Accounting for Leases,* or money-over-money and wrap lease transactions involving nonrecourse debt subject to the provisions of FASB Technical Bulletin No. 88-1, *Issues Relating to Accounting for Leases.* This Statement does not address transfers of nonfinancial assets, for example, servicing assets, or transfers of unrecognized financial assets, for example, minimum lease payments to be received under operating leases.

5. The Board concluded that an objective in accounting for transfers of financial assets is for each entity that is a party to the transaction to recognize only assets it controls and liabilities it has incurred, to **derecognize** assets only when control has been surrendered, and to derecognize liabilities only when they have been extinguished. Sales and other transfers may ~~frequently~~ result in a disaggregation of financial assets and liabilities into components, which become separate assets and liabilities. ~~For example, if an entity sells a portion of a financial asset it owns, the portion that continues to be held by a transferor becomes an asset separate from the portion sold and from the assets obtained in exchange.~~

6. The Board concluded that another objective is that recognition of financial assets and liabilities should not be affected by the sequence of transactions that result in their acquisition or incurrence unless the effect of those transactions is to maintain effective control over a transferred financial asset. For example, if a transferor sells financial assets it owns and at the same time writes an "at-the-money" put option (such as a guarantee or recourse obligation) on those assets, it should recognize the put obligation in the same manner as would another unrelated entity that writes an identical put option on assets it never owned. Similarly, a creditor may release a debtor on the condition that a third party assumes the obligation and that the original debtor becomes secondarily liable. In those circumstances, the original debtor becomes a guarantor and should recognize a guarantee obligation in the same manner as would a third-party guarantor that had never been primarily liable to that creditor, whether or not explicit consideration was paid for that guarantee. However, certain agreements to repurchase or redeem transferred financial assets maintain effective control over those assets and should therefore be accounted for differently than agreements to acquire assets never owned.

7. Before FASB Statement No. 125, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* accounting standards generally required that a transferor account for financial assets transferred as an inseparable unit that had been either entirely sold or entirely retained. Those standards were difficult to apply and produced inconsistent and arbitrary results. For example, whether a transfer "purported to be a sale" was sufficient to determine whether the transfer was accounted for and reported as a sale of receivables under one accounting standard or as a secured borrowing under another. After studying many of the complex developments that have occurred in financial markets leading up to the issuance of Statement 125 ~~during recent years~~, the Board concluded that previous approaches that viewed each financial asset as an indivisible unit do not provide an appropriate basis for developing consistent and operational standards for dealing with transfers and servicing of financial assets and extinguishments of liabilities. To address those issues adequately and consistently, the Board decided to adopt as the basis for ~~this~~ Statements 125 and 140 a *financial-components approach* that focuses on control and recognizes that financial assets and liabilities can be divided into a variety of components.

7A. The Board received a number of requests after the issuance of Statement 125 to reconsider or clarify the conditions for sale accounting and to expand the disclosure requirements of that Statement. In response to those requests, the Board decided to replace Statement 125 with Statement 140, even though the financial-components approach and many other provisions of Statement 125 were carried forward without reconsideration.

7B. However, after this Statement was issued, the Board received a number of requests from financial statement users and regulators to reconsider whether limits should be placed on the application of the financial-components approach to transfers of portions of a financial asset when the transferor also has significant continuing involvement with the transferred financial assets and continues to hold custody of the original financial assets. The Board continued to receive requests from financial statement users, regulators, preparers, and auditors to address other application issues. Other matters that the Board was asked to reconsider or clarify included:

a. The permitted activities of qualifying special-purpose entities
b. Isolation analysis
c. Effective control
d. The initial measurement of the transferor's interests in transferred financial assets
e. Disclosures.

7C. The Board decided to undertake a project to amend this Statement to address those concerns. The Board issued FASB Statement No. 166, *Accounting for Transfers of Financial Assets,* in June 2009 to amend this Statement. Statement 166 modifies the financial-components approach and also removes the concept of a qualifying special-purpose entity, clarifies the isolation and effective control conditions for sale accounting in paragraph 9, amends initial measurement of a transferor's interest in transferred financial assets, and requires additional disclosures. The Board also undertook a project to amend FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities,* due in part to the elimination of the qualifying special-purpose entity concept and the expectation that many **securitization** entities previously exempt from Interpretation 46(R) would become subject to its provisions. That project resulted in FASB Statement No. 167, *Amendments to FASB Interpretation No. 46(R),* which was issued together with Statement 166 in June 2009.

~~8. The Board issued Statement 125 in June 1996. After the issuance of that Statement, several parties called for reconsideration or clarification of certain provisions. Matters the Board was asked to reconsider or clarify included:~~

~~a. Circumstances in which a special-purpose entity (SPE) can be considered qualifying~~
~~b. Circumstances in which the assets held by a qualifying SPE should appear in the consolidated financial statements of the transferor~~
~~c. Whether sale accounting is precluded if the transferor holds a right to repurchase transferred assets that is attached to, is embedded in, or is otherwise transferable with the financial assets~~
~~d. Circumstances in which sale accounting is precluded if transferred financial assets can be removed from an SPE by the transferor (for example, under a removal-of-accounts provision (ROAP))~~
~~e. Whether arrangements that obligate, but do not entitle, a transferor to repurchase or redeem transferred financial assets should affect the accounting for those transfers~~
~~f. The impact of the powers of the Federal Deposit Insurance Corporation (FDIC) on isolation of assets transferred by financial institutions~~
~~g. Whether transfers of financial assets measured using the equity method of accounting should continue to be included in the scope of Statement 125~~
~~h. Whether disclosures should be enhanced to provide more information about assumptions used to determine the fair value of retained interests and the gain or loss on financial assets sold in securitizations~~
~~i. The accounting for and disclosure about collateral that can be sold or repledged.~~

~~The Board concluded that those requests to reconsider certain provisions of Statement 125 were appropriate and added a project to amend Statement 125 to its agenda in March 1997. This Statement is the result. To present the amended accounting standards for transfers of financial assets more clearly, this Statement replaces Statement 125. However, most of the provisions of Statement 125 have been carried forward without reconsideration.~~

STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

Accounting for Transfers and Servicing of Financial Assets

8A. The objective of paragraph 9 and related implementation guidance is to determine whether a transferor and its **consolidated affiliates** included in the financial statements being presented have surrendered control over transferred financial assets. This determination must consider the transferor's continuing involvement in the transferred financial assets and requires the use of judgment that must consider all arrangements or agreements made contemporaneously with, or in contemplation of, the transfer, even if they were not entered into at the time of the transfer.

8B. The requirements of paragraph 9 apply to transfers of an entire financial asset, transfers of a group of entire financial assets, and transfers of a **participating interest** in an entire financial asset (all of which are referred to collectively in this Statement as *transferred financial assets*). A participating interest has all of the following characteristics:

a. From the date of the transfer, it represents a proportionate (pro rata) ownership interest in an entire financial asset. The percentage of ownership interests held by the transferor in the entire financial asset may vary over time, while the entire financial asset remains outstanding as long as the resulting portions held by the transferor (including any participating interest retained by the transferor, its consolidated affiliates included in the financial statements being presented, or its **agents**) and the transferee(s) meet the other characteristics of a participating interest. For example, if the transferor's interest in an entire financial asset changes because it subsequently sells another interest in the entire financial asset, the interest held initially and subsequently by the transferor must meet the definition of a participating interest.
b. From the date of the transfer, all cash flows received from the entire financial asset are divided proportionately among the participating interest holders in an amount equal to their share of ownership. Cash flows allocated as compensation for services performed, if any, shall not be included in that determination provided those cash flows are not subordinate to the proportionate cash flows of the participating interest and are not significantly above an amount that would fairly compensate a substitute service provider, should one be required, which includes the profit that would be demanded in the marketplace. In addition, any cash flows received by the transferor as **proceeds** of the transfer of the participating interest shall be excluded from the determination of proportionate cash flows provided that the transfer does not result in the transferor receiving an ownership interest in the financial asset that permits it to receive disproportionate cash flows.
c. The rights of each participating interest holder (including the transferor in its role as a participating interest holder) have the same priority, and no participating interest holder's interest is subordinated to the interest of another participating interest holder. That priority does not change in the event of bankruptcy or other receivership of the transferor, the original debtor, or any other participating interest holder. Participating interest holders have no recourse to the transferor (or its consolidated affiliates included in the financial statements being presented or its agents) or to each other, other than **standard representations and warranties,** ongoing contractual obligations to service the entire financial asset and administer the transfer contract, and contractual obligations to share in any set-off benefits received by any participating interest holder. That is, no participating interest holder is entitled to receive cash before any other participating interest holder under its contractual rights as a participating interest holder. For example, if a participating interest holder also is the servicer of the entire financial asset and receives cash in its role as servicer, that arrangement would not violate this requirement.
d. No party has the right to pledge or exchange the entire financial asset unless all participating interest holders agree to pledge or exchange the entire financial asset.

If a transfer of a portion of an entire financial asset meets the definition of a participating interest, the transferor shall apply the guidance in paragraph 9. If a transfer of a portion of a financial asset does not meet the definition of a participating interest, the transferor and transferee shall account for the transfer in accordance with the guidance in paragraph 12. However, if the transferor transfers an entire financial asset in portions that do not individually meet the participating interest definition, paragraph 9 shall be applied to the entire financial asset once all portions have been transferred.

9. A transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset ~~financial assets (or all or a portion of a financial asset)~~ in which the transferor surrenders control over those financial assets shall be accounted for as a sale ~~to the extent that consideration other than **beneficial interests** in the transferred assets is received in exchange. The transferor has surrendered control over transferred assets~~ if and only if *all of the following conditions* are met:

a. The transferred financial assets have been isolated from the transferor—put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership~~ (paragraphs 27 and 28)~~. Transferred financial assets are isolated in bankruptcy or other receivership only if the transferred financial assets would be beyond the reach of the powers of a bankruptcy trustee or other receiver for the transferor or any of its consolidated affiliates included in the financial statements being presented. For multiple step transfers, an entity that is designed to make remote the possibility that it would enter bankruptcy or other receivership (bankruptcy-remote entity) is not considered a consolidated affiliate for purposes of performing the isolation analysis. Notwithstanding the isolation analysis, each entity involved in the transfer is subject to the applicable guidance on whether it must be consolidated (paragraphs 27–28 and 80–84).

b. Each transferee (or, if the transferee is an entity whose sole purpose is to engage in securitization or asset-backed financing activities and that entity is constrained from pledging or exchanging the assets it receives~~ a qualifying SPE (paragraph 35)~~, each third-party holder of its beneficial interests) has the right to pledge or exchange the assets (or beneficial interests) it received, and no condition both constrains the transferee (or third-party holder of its beneficial interests) from taking advantage of its right to pledge or exchange and provides more than a trivial benefit to the transferor (paragraphs 29–33~~29–34~~).

c. The transferor, its consolidated affiliates included in the financial statements being presented, or its agents doe~~s~~ not maintain effective control over the transferred financial assets or third-party beneficial interests related to those transferred assets (paragraph 46A). Examples of a transferor's effective control over the transferred financial assets include, but are not limited to ~~through either~~ (1) an agreement that both entitles and obligates the transferor to repurchase or redeem them before their maturity (paragraphs 47–49),~~ or~~ (2) an agreement that provides the transferor with both the ~~ability to unilaterally~~ **unilateral ability** to cause the holder to return specific financial assets and a more-than-trivial benefit attributable to that ability, other than through a **cleanup call** (paragraphs 50–54), or (3) an agreement that permits the transferee to require the transferor to repurchase the transferred financial assets at a price that is so favorable to the transferee that it is probable that the transferee will require the transferor to repurchase them (paragraph 54A).

Accounting for Transfers of Participating Interests

10. ~~Upon completion of any transfer of financial assets, the transferor shall:~~

~~a. Initially recognize and measure at fair value, if practicable (paragraph 71), servicing assets and servicing liabilities that require recognition under the provisions of paragraph 13~~

~~b. Allocate the previous carrying amount between the assets sold, if any, and the interests that continue to be held by the transferor, if any, based on their relative fair values at the date of transfer (paragraphs 56–60)~~

~~c. Continue to carry in its statement of financial position any interest it continues to hold in the transferred assets, including, if applicable, beneficial interests in assets transferred to a qualifying SPE in a **securitization** (paragraphs 73–84), and any **undivided interests** (paragraphs 58 and 59).~~

Upon completion[2a] of a transfer of a participating interest that satisfies the conditions to be accounted for as a sale (paragraph 9), the transferor (**seller**) shall:

a. Allocate the previous carrying amount of the entire financial asset between the participating interests sold and the participating interest that continues to be held by the transferor on the basis of their relative fair values at the date of the transfer (paragraphs 58 and 60)
b. Derecognize the participating interest(s) sold
c. Recognize and initially measure at fair value servicing assets, servicing liabilities, and any other assets obtained and liabilities incurred in the sale (such as cash) (paragraphs 61–64)
d. Recognize in earnings any gain or loss on the sale
e. Report any participating interest or interests that continue to be held by the transferor as the difference between the previous carrying amount of the entire financial asset and the amount derecognized.

The transferee shall recognize the participating interest(s) obtained, other assets obtained, and any liabilities incurred and initially measure them at fair value.

[2a]Although a transfer of securities may not be considered to be completed until the settlement date, this Statement does not modify other generally accepted accounting principles (GAAP), including FASB Statement No. 35, *Accounting and Reporting by Defined Benefit Pension Plans,* and AICPA Statements of Position and Audit and Accounting Guides for certain industries that require accounting at the trade date for certain contracts to purchase or sell securities.

10A. Upon completion of a transfer of participating interests that does not satisfy the conditions to be accounted for as a sale, the guidance in paragraph 12 shall be applied.

Accounting for Transfers of an Entire Financial Asset or Group of Entire Financial Assets

11. Upon completion[3] of a transfer of an entire financial assets or a group of entire financial assets that satisfies the conditions to be accounted for as a sale (paragraph 9), the transferor (seller) shall:

a. Derecognize ~~all~~ the transferred financial assets ~~sold~~
~~b. Recognize all assets obtained and liabilities incurred in consideration as **proceeds** of the sale, including cash, put or call options held or written (for example, guarantee or recourse obligations), forward commitments (for example, commitments to deliver additional receivables during the revolving periods of some securitizations), swaps (for example, provisions that convert interest rates from fixed to variable), and servicing assets and servicing liabilities, if applicable (paragraphs 56, 57, and 61–67)~~
c. Recognize and i~~I~~nitially measure at fair value servicing assets, servicing liabilities, and any other assets obtained (including a transferor's beneficial interest in the transferred financial assets) and liabilities incurred[3a] in the sale (paragraphs 56, 57, and 61–65)~~a sale or, if it is not practicable to estimate the fair value of an asset or a liability, apply alternative measures (paragraphs 71 and 72)~~
d. Recognize in earnings any gain or loss on the sale.

The transferee shall recognize all assets obtained and any liabilities incurred and initially measure them at fair value ~~(in aggregate, presumptively the price paid)~~.

11A. Upon completion of a transfer of an entire financial asset or a group of entire financial assets that does not satisfy the conditions to be accounted for as a sale in its entirety, the guidance in paragraph 12 shall be applied.

Secured Borrowing

12. If a transfer of an entire financial asset~~s~~, a group of entire financial assets, or a participating interest in an entire financial asset ~~in exchange for cash or other consideration (other than beneficial interests in the transferred assets)~~ does not meet the ~~criteria~~ conditions for a sale in paragraph 9~~,~~ or if a transfer of a portion of an entire financial asset does not meet the definition of a participating interest (paragraph 8B), the transferor and transferee shall account for the transfer as a secured borrowing with pledge of collateral (paragraph 15). The transferor shall continue to report the transferred financial assets in its statement of financial position with no change in their measurement (that is, basis of accounting).

Recognition and Measurement of Servicing Assets and Servicing Liabilities

13. An entity shall recognize and initially measure at fair value~~, if practicable,~~ a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in either ~~any~~ of the following situations:

a. A servicer's transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset ~~the servicer's financial assets~~ that meets the requirements for sale accounting; or
~~b. A transfer of the servicer's financial assets to a qualifying SPE in a **guaranteed mortgage securitization** in which the transferor retains all of the resulting securities and classifies them as either available-for-sale securities or trading securities in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*~~
c. An acquisition or assumption of a servicing obligation that does not relate to financial assets of the servicer or its consolidated affiliates included in the financial statements being presented.

An entity that transfers its financial assets ~~to a qualifying SPE in a guaranteed mortgage securitization~~ to an unconsolidated entity in a transfer that qualifies as

[3]See footnote 2a.~~Although a transfer of securities may not be considered to have reached completion until the settlement date, this Statement does not modify other generally accepted accounting principles, including FASB Statement No. 35, *Accounting and Reporting by Defined Benefit Pension Plans,* and AICPA Statements of Position and audit and accounting Guides for certain industries, that require accounting at the trade date for certain contracts to purchase or sell securities.~~

[3a]Some assets that might be obtained and liabilities that might be incurred include cash, put or call options that are held or written (for example, guarantee or recourse obligations), forward commitments (for example, commitments to deliver additional receivables during the revolving periods of some securitizations), and swaps (for example, provisions that convert interest rates from fixed to variable).

a sale in which the transferor ~~retains all of~~ obtains the resulting securities and classifies them as debt securities held-to-maturity in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* may either separately recognize its servicing assets or servicing liabilities or report those servicing assets or servicing liabilities together with the asset being serviced.

13A. An entity shall subsequently measure each class of servicing assets and servicing liabilities using one of the following methods:

a. *Amortization method:* Amortize servicing assets or servicing liabilities in proportion to and over the period of estimated net servicing income (if servicing revenues exceed servicing costs) or net servicing loss (if servicing costs exceed servicing revenues), and assess servicing assets or servicing liabilities for impairment or increased obligation based on fair value at each reporting date
b. *Fair value measurement method:* Measure servicing assets or servicing liabilities at fair value at each reporting date and report changes in fair value of servicing assets and servicing liabilities in earnings in the period in which the changes occur.

The election described in this paragraph shall be made separately for each class of servicing assets and servicing liabilities. An entity shall apply the same subsequent measurement method to each servicing asset and servicing liability in a class. Classes of servicing assets and servicing liabilities shall be identified based on (a) the availability of market inputs used in determining the fair value of servicing assets or servicing liabilities, (b) an entity's method for managing the risks of its servicing assets or servicing liabilities, or (c) both. Once an entity elects the fair value measurement method for a class of servicing assets and servicing liabilities, that election shall not be reversed (paragraph 63). ~~If it is not practicable to initially measure a servicing asset or servicing liability at fair value, an entity shall initially recognize the servicing asset or servicing liability in accordance with paragraph 71 and shall include it in a class subsequently measured using the amortization method.~~

13B. An entity shall report recognized servicing assets and servicing liabilities that are subsequently measured using the fair value measurement method in a manner that separates those carrying amounts on the face of the statement of financial position from the carrying amounts for separately recognized servicing assets and servicing liabilities that are subsequently measured using the amortization method. To accomplish that separate reporting, an entity may either (a) display separate line items for the amounts that are subsequently measured using the fair value measurement method and amounts that are subsequently measured using the amortization method or (b) present the aggregate of those amounts that are subsequently measured at fair value and those amounts that are subsequently measured using the amortization method (paragraph 63) and disclose parenthetically the amount that is subsequently measured at fair value that is included in the aggregate amount.

Financial Assets Subject to Prepayment

14. Financial assets, except for instruments that are within the scope of Statement 133, that can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment shall be subsequently measured like investments in debt securities classified as available-for-sale or trading under Statement 115. Examples of such financial assets include, but are not limited to, interest-only strips, other beneficial interests~~Interest-only strips, other interests that continue to be held by a transferor in securitizations~~, loans, or other receivables~~, or other financial assets that can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment, except for instruments that are within the scope of Statement 133, shall be subsequently measured like investments in debt securities classified as available-for-sale or trading under Statement 115, as amended (paragraph 362)~~.

Secured Borrowings and Collateral

15. A debtor may grant a **security interest** in certain assets to a lender (the secured party) to serve as collateral for its obligation under a borrowing, with or without recourse to other assets of the debtor. An obligor under other kinds of current or potential obligations, for example, interest rate swaps, also may grant a security interest in certain assets to a secured party. If collateral is transferred to the secured party, the custodial arrangement is commonly referred to as a pledge. Secured parties sometimes are permitted to sell or repledge (or otherwise transfer) collateral held under a pledge. The same relationships occur, under different names, in transfers documented as sales

that are accounted for as secured borrowings (paragraph 12). The accounting for noncash[4] collateral by the debtor (or obligor) and the secured party depends on whether the secured party has the right to sell or repledge the collateral and on whether the debtor has defaulted.

a. If the secured party (transferee) has the right by contract or custom to sell or repledge the collateral, then the debtor (transferor) shall reclassify that asset and report that asset in its statement of financial position separately (for example, as security pledged to creditors) from other assets not so encumbered.
b. If the secured party (transferee) sells collateral pledged to it, it shall recognize the proceeds from the sale and its obligation to return the collateral. The sale of the collateral is a transfer subject to the provisions of this Statement.
c. If the debtor (transferor) defaults under the terms of the secured contract and is no longer entitled to redeem the pledged asset, it shall derecognize the pledged asset, and the secured party (transferee) shall recognize the collateral as its asset initially measured at fair value or, if it has already sold the collateral, derecognize its obligation to return the collateral.
d. Except as provided in paragraph 15(c), the debtor (transferor) shall continue to carry the collateral as its asset, and the secured party (transferee) shall not recognize the pledged asset.

Extinguishments of Liabilities

16. A debtor shall derecognize a liability if and only if it has been extinguished. A liability has been extinguished if either of the following conditions is met:

a. The debtor pays the creditor and is relieved of its obligation for the liability. Paying the creditor includes delivery of cash, other financial assets, goods, or services or reacquisition by the debtor of its outstanding debt securities whether the securities are canceled or held as so-called treasury bonds.
b. The debtor is legally released[5] from being the primary obligor under the liability, either judicially or by the creditor.

Disclosures

~~*Disclosures for Public Entities*~~

16A. ~~In addition to the disclosures required by other standards, a public entity[5a] shall provide disclosures as required in Appendix B of FASB Staff Position (FSP) FAS 140-4 and FIN 46(R)-8, *Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities*~~ The principal objectives of the disclosures required by this Statement are to provide users of the financial statements with an understanding of all of the following:

a. A transferor's continuing involvement (as defined in the glossary of this Statement), if any, with transferred financial assets
b. The nature of any restrictions on assets reported by an entity in its statement of financial position that relate to a transferred financial asset, including the carrying amounts of those assets
c. How servicing assets and servicing liabilities are reported under this Statement

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[4]Cash "collateral," sometimes used, for example, in securities lending transactions (paragraphs 91–95), shall be derecognized by the payer and recognized by the recipient, not as collateral, but rather as proceeds of either a sale or a borrowing.

[5]If nonrecourse debt (such as certain mortgage loans) is assumed by a third party in conjunction with the sale of an asset that serves as sole collateral for that debt, the sale and related assumption effectively accomplish a legal release of the seller-debtor for purposes of applying this Statement.

~~[5a]The following definitions of public and nonpublic shall be applied in assessing whether an entity is public or nonpublic:~~

~~**Nonpublic entity—**Any entity other than one (a) whose debt or equity securities trade in a public market either on a stock exchange (domestic or foreign) or in the over-the-counter market, including securities quoted only locally or regionally, (b) that is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets), (c) that makes a filing with a regulatory agency in preparation for the sale of any class of debt or equity securities in a public market, or (d) that is controlled by an entity covered by (a), (b), or (c).~~

~~*Conduit debt securities* refers to certain limited-obligation revenue bonds, certificates of participation, or similar debt instruments issued by a state or local governmental entity for the express purpose of providing financing for a specific third party (the conduit bond obligor) that is not a part of the state or local government's financial reporting entity. Although conduit debt securities bear the name of the governmental entity that issues them, the governmental entity often has no obligation for such debt beyond the resources provided by a lease or loan agreement with the third party on whose behalf the securities are issued. Further, the conduit bond obligor is responsible for any future financial reporting requirements.~~

~~**Public entity—**Any entity that does not meet the definition of a *nonpublic entity*.~~

d. For transfers accounted for as sales when a transferor has continuing involvement with the transferred financial assets and for transfers of financial assets accounted for as secured borrowings, how the transfer of financial assets affects a transferor's financial position, financial performance, and cash flows.

Those objectives apply regardless of whether this Statement requires specific disclosures. The specific disclosures required by this Statement are minimum requirements and an entity may need to supplement the required disclosures specified in paragraph 17 depending on the facts and circumstances of a transfer, the nature of an entity's continuing involvement with the transferred financial assets, and the effect of an entity's continuing involvement on the transferor's financial position, financial performance, and cash flows. Disclosures required by other U.S. generally accepted accounting principles (GAAP) for a particular form of continuing involvement shall be considered when determining whether the disclosure objectives of this Statement have been met.

~~Disclosures for Nonpublic Entities~~

16B. Disclosures required by this Statement may be reported in the aggregate for similar transfers if separate reporting of each transfer would not provide more useful information to financial statement users. A transferor shall disclose how similar transfers are aggregated. A transferor shall distinguish transfers that are accounted for as sales from transfers that are accounted for as secured borrowings. In determining whether to aggregate the disclosures for multiple transfers, the reporting entity shall consider quantitative and qualitative information about the characteristics of the transferred financial assets. For example, consideration should be given, but not limited, to the following:

a. The nature of the transferor's continuing involvement
b. The types of financial assets transferred
c. Risks related to the transferred financial assets to which the transferor continues to be exposed after the transfer and the change in the transferor's risk profile as a result of the transfer
d. The requirements of FSP SOP 94-6-1, *Terms of Loan Products That May Give Rise to a Concentration of Credit Risk.*

16C. The disclosures shall be presented in a manner that clearly and fully explains to financial statement users the transferor's risk exposure related to the transferred financial assets and any restrictions on the assets of the entity. An entity shall determine, in light of the facts and circumstances, how much detail it must provide to satisfy the disclosure requirements of this Statement and how it aggregates information for assets with different risk characteristics. The entity must strike a balance between obscuring important information as a result of too much aggregation and excessive detail that may not assist financial statement users to understand the entity's financial position. For example, an entity shall not obscure important information by including it with a large amount of insignificant detail. Similarly, an entity shall not disclose information that is so aggregated that it obscures important differences between the different types of involvement or associated risks.

16D. The disclosures in paragraph 17(f) of this Statement apply to transfers accounted for as sales when the transferor has continuing involvement with transferred financial assets as a result of a securitization, asset-backed financing arrangement, or a similar transfer. If specific disclosures are required for a particular form of the transferor's continuing involvement by other U.S. GAAP, the transferor shall provide the information required in paragraphs 17(f)(1)(a) and 17(f)(2)(a) of this Statement with a cross-reference to the separate notes to financial statements so a financial statement user can understand the risks retained in the transfer. The entity need not provide each specific disclosure required in paragraphs 17(f)(1)(b), 17(f)(2)(a)(i)–(iv), and 17(f)(2)(b)–(e) if the disclosure is not required by other U.S. GAAP and the objectives of paragraph 16A are met. For example, if the transferor's only form of continuing involvement is a derivative, the entity shall provide the disclosures required in paragraphs 17(f)(1)(a) and 17(f)(2)(a) of this Statement and the disclosures about derivatives required by applicable U.S. GAAP. In addition, the entity would evaluate whether the other disclosures in paragraph 17(f) are necessary for the entity to meet the objectives in paragraph 16A.

16E. To apply the disclosures in paragraph 17, an entity shall consider all involvements by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents to be involvements by the transferor.

17. An entity shall disclose the following:

a. For collateral:
   (1) If the entity has entered into repurchase agreements or securities lending transactions, its policy for requiring collateral or other security.
   (2) If the entity has pledged any of its assets as collateral that are not reclassified and separately reported in the statement of financial position pursuant to paragraph 15(a), the carrying amounts and classifications of both those assets and associated liabilities as of the date of the latest statement of financial position presented, including qualitative information about the relationship(s) between those assets and associated liabilities. For example, if assets are restricted solely to satisfy a specific obligation, the carrying amounts of those assets and associated liabilities, including a description of the nature of restrictions placed on the assets, shall be disclosed.
   (3) If the entity has accepted collateral that it is permitted by contract or custom to sell or repledge, the fair value as of the date of each statement of financial position presented of that collateral and of the portion of that collateral that it has sold or repledged, and information about the sources and uses of that collateral.

b. For in-substance defeasance of debt:
   ~~b.~~(1) If debt was considered to be extinguished by in-substance defeasance under the provisions of FASB Statement No. 76, *Extinguishment of Debt,* prior to the effective date of Statement 125,[6] a general description of the transaction and the amount of debt that is considered extinguished at the end of each ~~the~~ period ~~so long as~~ that debt remains outstanding.

~~c. If assets are set aside after the effective date of Statement 125 solely for satisfying scheduled payments of a specific obligation, a description of the nature of restrictions placed on those assets.~~

~~d. If it is not practicable to estimate the fair value of certain assets obtained or liabilities incurred in transfers of financial assets during the period, a description of those items and the reasons why it is not practicable to estimate their fair value.~~

~~e~~c. For all servicing assets and servicing liabilities:
   (1) Management's basis for determining its classes of servicing assets and servicing liabilities (paragraph 13A).
   (2) A description of the risks inherent in servicing assets and servicing liabilities and, if applicable, the instruments used to mitigate the income statement effect of changes in fair value of the servicing assets and servicing liabilities. (Disclosure of quantitative information about the instruments used to manage the risks inherent in servicing assets and servicing liabilities, including the fair value of those instruments at the beginning and end of the period, is encouraged but not required.)
   (3) The amount of **contractually specified servicing fees** ~~(as defined in the glossary)~~, late fees, and ancillary fees earned for each period for which results of operations are presented, including a description of where each amount is reported in the statement of income.
   (4) Quantitative and qualitative information about the assumptions used to estimate the fair value (for example, discount rates, anticipated credit losses, and prepayment speeds). (An entity that provides quantitative information about the instruments used to manage the risks inherent in the servicing assets and servicing liabilities, as encouraged by paragraph 17(c)(2), also is encouraged, but not required, to disclose quantitative and qualitative information about the assumptions used to estimate the fair value of those instruments.)

~~f~~d. For servicing assets and servicing liabilities subsequently measured at fair value:
   (1) For each class of servicing assets and servicing liabilities, the activity in the balance of servicing assets and the activity in the balance of servicing liabilities (including a description of where changes in fair value are reported in the statement of income for each period for which results of operations are

[6]Statement 125 applied to transfers and servicing of financial assets and extinguishments of liabilities occurring after December 31, 1996 (after December 31, 1997, for transfers affected by FASB Statement No. 127, *Deferral of the Effective Date of Certain Provisions of FASB Statement No. 125*) and on or before March 31, 2001. Statement 127 deferred until December 31, 1997, 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.~~Refer to footnote 11 to paragraph 19.~~

presented), including, but not limited to, the following:
- (a) The beginning and ending balances
- (b) Additions (through purchases of servicing assets, assumptions of servicing obligations, and recognition of servicing obligations that result from transfers of financial assets)
- (c) Disposals
- (d) Changes in fair value during the period resulting from:
  - (i) Changes in valuation inputs or assumptions used in the valuation model
  - (ii) Other changes in fair value and a description of those changes
- (e) Other changes that affect the balance and a description of those changes.

~~(2) A description of the valuation techniques or other methods used to estimate the fair value of servicing assets and servicing liabilities. If a valuation model is used, the description shall include the methodology and model validation procedures, as well as quantitative and qualitative information about the assumptions used in the valuation model (for example, discount rates and prepayment speeds). (An entity that provides quantitative information about the instruments used to manage the risks inherent in the servicing assets and servicing liabilities, as encouraged by paragraph 17(e)(2), is also encouraged, but not required, to disclose a description of the valuation techniques, as well as quantitative and qualitative information about the assumptions used to estimate the fair value of those instruments.)~~

~~g~~e. For servicing assets and servicing liabilities subsequently amortized in proportion to and over the period of estimated net servicing income or loss and assessed for impairment or increased obligation:

(1) For each class of servicing assets and servicing liabilities, the activity in the balance of servicing assets and the activity in the balance of servicing liabilities (including a description of where changes in the carrying amount are reported in the statement of income for each period for which results of operations are presented), including, but not limited to, the following:
- (a) The beginning and ending balances
- (b) Additions (through purchases of servicing assets, assumptions of servicing obligations, and recognition of servicing obligations that result from transfers of financial assets)
- (c) Disposals
- (d) Amortization
- (e) Application of valuation allowance to adjust carrying value of servicing assets
- (f) Other-than-temporary impairments
- (g) Other changes that affect the balance and a description of those changes.

(2) For each class of servicing assets and servicing liabilities, the fair value of recognized servicing assets and servicing liabilities at the beginning and end of the period~~ if it is practicable to estimate the value~~.

~~(3) A description of the valuation techniques or other methods used to estimate fair value of the servicing assets and servicing liabilities. If a valuation model is used, the description shall include the methodology and model validation procedures, as well as quantitative and qualitative information about the assumptions used in the valuation model (for example, discount rates, and prepayment speeds). (An entity that provides quantitative information about the instruments used to manage the risks inherent in the servicing assets and servicing liabilities, as encouraged by paragraph 17(e)(2), is also encouraged, but not required, to disclose a description of the valuation techniques as well as quantitative and qualitative information about the assumptions used to estimate the fair value of those instruments.)~~

(~~4~~3) The risk characteristics of the underlying financial assets used to stratify recognized servicing assets for purposes of measuring impairment in accordance with paragraph 63.

(~~5~~4) The activity by class in any valuation allowance for impairment of recognized servicing assets—including beginning and ending balances, aggregate additions charged and recoveries credited to operations, and aggregate write-downs charged against the allowance—for each period for which results of operations are presented.

~~h~~f. ~~If the entity has securitized~~For securitizations, asset-backed financing arrangements, and similar transfers accounted for as sales when the transferor has continuing involvement (as defined in the glossary) with the transferred financial assets ~~during any period presented and accounts for that transfer as a sale, for each major asset type (for example, mortgage loans, credit card receivables, and automobile loans)~~:

(1) For each income statement presented:~~Its accounting policies for initially measuring the interests that continue to be held by the transferor, if any, and servicing assets or servicing liabilities, if any, including the methodology (whether quoted market price, prices based on sales of similar assets and liabilities, or prices based on valuation techniques) used in determining their fair value.~~

(~~2~~a) The characteristics of the transfer ~~securitizations~~ (including a description of the transferor's continuing involvement with the transferred financial assets, and the nature and initial fair value of the assets obtained as proceeds and the liabilities incurred in the transfer ~~including, but not limited to, servicing, recourse, and restrictions on interests that continue to be held by the trans-feror~~) and the gain or loss from sale of transferred financial assets ~~in securitizations~~. For initial fair value measurements of assets obtained and liabilities incurred in the transfer, the following information:

(i) The level within the fair value hierarchy (as described in FASB Statement No. 157, *Fair Value Measurements*) in which the fair value measurements in their entirety fall, segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3)

(~~3~~ii) The key inputs and assumptions[7] used in measuring the fair value of assets obtained and liabilities incurred as a result of the sale ~~interests that continue to be held by the transferor and servicing assets or servicing liabilities, if any, at the time of securitization~~ that relate to the transferor's continuing involvement (including, at a minimum, but not limited to, and if applicable, quantitative information about discount rates, expected prepayments including the expected weighted-average life of prepayable financial assets,[8] and anticipated credit losses, ~~if applicable~~including expected static pool losses[8a])[8b]

(iii) The valuation technique(s) used to measure fair value.

(~~4~~b) Cash flows between a transferor and transferee, ~~the securitization SPE and the transferor, unless reported separately elsewhere in the financial statements or notes (~~including proceeds from new transfers ~~securitizations~~, proceeds from collections reinvested in revolving-period transfers ~~securitizations~~, purchases of previously transferred financial assets ~~delinquent or foreclosed loans~~, servicing fees, and cash flows received ~~on~~ from a transferor's beneficial interests ~~that continue to be held by the transferor~~).

~~i.~~(2) For each statement of financial position presented, regardless of when the transfer occurred:~~If the entity has interests that continue to be held by the transferor in financial~~

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[7]If an entity has aggregated ~~made~~ multiple ~~securitizations of the same major asset type~~ transfers during a period in accordance with paragraphs 16B and 16C, it may disclose the range of assumptions.

[8]The weighted-average life of prepayable assets in periods (for example, months or years) can be calculated by multiplying the principal collections expected in each future period by the number of periods until that future period, summing those products, and dividing the sum by the initial principal balance.

[8a]Expected static pool losses can be calculated by summing the actual and projected future credit losses and dividing the sum by the original balance of the pool of assets.

[8b]The timing and amount of future cash flows for transferor's interests in transferred financial assets are commonly uncertain, especially if those interests are subordinate to more senior beneficial interests. Thus, estimates of future cash flows used for a fair value measurement depend heavily on assumptions about default and prepayment of all the financial assets transferred, because of the implicit credit or prepayment risk enhancement arising from the subordination.

~~assets that it has securitized or servicing assets or servicing liabilities relating to assets that it has securitized, at the date of the latest statement of financial position presented, for each major asset type (for example, mortgage loans, credit card receivables, and automobile loans):~~

(a) Qualitative and quantitative information about the transferor's continuing involvement with transferred financial assets that provides financial statement users with sufficient information to assess the reasons for the continuing involvement and the risks related to the transferred financial assets to which the transferor continues to be exposed after the transfer and the extent that the transferor's risk profile has changed as a result of the transfer (including, but not limited to, credit risk, interest rate risk, and other risks), including:

(i) The total principal amount outstanding, the amount that has been derecognized, and the amount that continues to be recognized in the statement of financial position

(ii) The terms of any arrangements that could require the transferor to provide financial support (for example, liquidity arrangements and obligations to purchase assets) to the transferee or its beneficial interest holders, including a description of any events or circumstances that could expose the transferor to loss and the amount of the maximum exposure to loss

(iii) Whether the transferor has provided financial or other support during the periods presented that it was not previously contractually required to provide to the transferee or its beneficial interest holders, including when the transferor assisted the transferee or its beneficial interest holders in obtaining support, including:

(1) The type and amount of support

(2) The primary reasons for providing the support

(iv) Information is encouraged about any liquidity arrangements, guarantees, and/or other commitments provided by third parties related to the transferred financial assets that may affect the transferor's exposure to loss or risk of the related transferor's interest.

(b~~1~~) The entity's ~~Its~~ accounting policies for subsequently measuring ~~those interests~~assets or liabilities that relate to the continuing involvement with the transferred financial assets~~, including the methodology (whether quoted market price, prices based on sales of similar assets and liabilities, or prices based on valuation techniques) used in determining their fair value~~

(c~~2~~) The key inputs and assumptions[8c] used in ~~subsequently~~ measuring the fair value of ~~those interests~~ assets or liabilities that relate to the transferor's continuing involvement (including, at a minimum, but not limited to, and if applicable, quantitative information about discount rates, expected prepayments including the expected weighted-average life of prepayable financial assets,[8d] and anticipated credit losses, including expected static pool losses~~,~~[9] ~~if applicable~~)[9a]

(d~~3~~) For the transferor's interests in the transferred financial assets, a~~A~~ sensitivity analysis or stress test showing the hypothetical effect on the fair value

[8c]See footnote 7.

[8d]See footnote 8.

[9]~~Expected static pool losses can be calculated by summing the actual and projected future credit losses and dividing the sum by the original balance of the pool of assets~~See footnote 8a.

[9a]~~The timing and amount of future cash flows for retained interests in securitizations are commonly uncertain, especially if those interests are subordinate to more senior beneficial interests. Thus, estimates of future cash flows used for a fair value measurement depend heavily on assumptions about default and prepayment of all the assets securitized, because of the implicit credit or prepayment risk enhancement arising from subordination~~See footnote 8b.

of those interests (including any servicing assets or servicing liabilities) of two or more unfavorable variations from the expected levels for each key assumption that is reported under paragraph 17(f)(2)(c) above independently from any change in another key assumption, and a description of the objectives, methodology, and limitations of the sensitivity analysis or stress test

(c~~4~~) Information about the asset quality of transferred financial assets and any other assets that it manages together with them. This information shall be separated between assets that have been derecognized and assets that continue to be recognized in the statement of financial position. This information is intended to provide financial statement users with an understanding of the risks inherent in the transferred financial assets as well as in other assets and liabilities that it manages together with transferred financial assets. For example, information for receivables shall include, but is not limited to:~~For the securitized assets and any other financial assets that it manages together with them:[10]~~

- ~~(a) The total principal amount outstanding, the portion that has been derecognized, and the portion that continues to be recognized in each category reported in the statement of financial position, at the end of the period~~
- (~~b~~i) Delinquencies at the end of the period
- (~~c~~ii) Credit losses, net of recoveries, during the period.

~~(Disclosure of average balances during the period is encouraged, but not required.)~~

g. Disclosure requirements for transfers of financial assets accounted for as secured borrowings:

(1) The carrying amounts and classifications of both assets and associated liabilities recognized in the transferor's statement of financial position at the end of each period presented, including qualitative information about the relationship(s) between those assets and associated liabilities. For example, if assets are restricted solely to satisfy a specific obligation, the carrying amounts of those assets and associated liabilities, including a description of the nature of restrictions placed on the assets.

Implementation Guidance

18. Appendix A describes certain provisions of this Statement in more detail and describes their application to certain types of transactions. Appendix A is an integral part of the standards provided in this Statement.

Effective Date and Transition

[Paragraphs 19–25 have been omitted because the effective dates of those provisions in this Statement have passed. For the transition and effective date provisions of these amendments, see paragraphs 5–7 of Statement 166.]

Appendix A

IMPLEMENTATION GUIDANCE

Introduction

26. This appendix describes certain provisions of this Statement in more detail and describes how they apply to certain types of transactions. This appendix discusses generalized situations. Facts and circumstances and specific contracts need to be considered carefully in applying this Statement. This appendix is an integral part of the standards provided in this Statement.

26A. Paragraph 8A of this Statement states that the objective of paragraph 9 and related implementation guidance is to determine whether a transferor and its consolidated affiliates included in the financial statements being presented have surrendered control over transferred financial assets. As a result, in determining whether the transferor has surrendered control over transferred financial assets, the transferor must first consider whether the transferee would be consolidated by the transferor. Therefore, if all other provisions of this Statement are met with respect to a

~~[10]Excluding securitized assets that an entity continues to service but with which it has no other continuing involvement.~~

particular transfer, and the transferee would be consolidated by the transferor, then the transferred financial assets would not be treated as having been sold in the financial statements being presented. However, if the transferee is a consolidated subsidiary of the transferor (its parent), the transferee shall recognize the transferred financial assets in its separate company financial statements, unless the nature of the transfer is a secured borrowing with a pledge of collateral (for example, a repurchase agreement that would not be accounted for as a sale under the provisions of paragraphs 47–49).

Unit of Account

26B. Paragraph 8B establishes the unit of account to which the sale accounting conditions in paragraph 9 shall be applied. Paragraph 8B states that paragraph 9 shall be applied to transfers of an entire financial asset, transfers of a group of entire financial assets, and transfers of a participating interest in an entire financial asset. Inherent in that principle is that to be eligible for sale accounting an entire financial asset cannot be divided into components before a transfer unless all of the components meet the definition of a participating interest.

26C. The legal form of the asset and what the asset conveys to its holders shall be considered in determining what constitutes an entire financial asset. The following examples illustrate the application of what constitutes an entire financial asset:

a. A loan to one borrower in accordance with a single contract that is transferred to a securitization entity before securitization shall be considered an entire financial asset. Similarly, a beneficial interest in securitized financial assets after the securitization process has been completed shall be considered an entire financial asset. In contrast, a transferred interest in an individual loan shall not be considered an entire financial asset; however, if the transferred interest meets the definition of a participating interest, the participating interest would be eligible for sale accounting.
b. In a transaction in which the transferor creates an interest-only strip from a loan and transfers the interest-only strip, the interest-only strip does not meet the definition of an entire financial asset (and an interest-only strip does not meet the definition of a participating interest; therefore, sale accounting would be precluded). In contrast, if an entire financial asset is transferred to a securitization entity that it does not consolidate and the transfer meets the conditions for sale accounting, the transferor may obtain an interest-only strip as proceeds from the sale. An interest-only strip received as proceeds of a sale is an entire financial asset for purposes of evaluating any future transfers that could then be eligible for sale accounting.
c. If multiple advances are made to one borrower in accordance with a single contract (such as a line of credit, credit card loan, or a construction loan), an advance on that contract would be a separate unit of account if the advance retains its identity, does not become part of a larger loan balance, and is transferred in its entirety. However, if the transferor transfers an advance in its entirety and the advance loses its identity and becomes part of a larger loan balance, the transfer would be eligible for sale accounting only if the transfer of the advance does not result in the transferor retaining any interest in the larger balance or if the transfer results in the transferor's interest in the larger balance meeting the definition of a participating interest. Similarly, if the transferor transfers an interest in an advance that has lost its identity, the interest must be a participating interest in the larger balance to be eligible for sale accounting.

Participating Interests in an Entire Financial Asset

26D. Paragraph 8B(b) requires that all cash flows received from the entire financial asset be divided among the participating interest holders (including any interest retained by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents) in proportion to their share of ownership. That is, the participating interest definition does not allow for the allocation of specified cash flows unless each cash flow is proportionately allocated to the participating interest holders. For example, in the case of an individual loan in which the borrower is required to make a contractual payment that consists of a principal amount and interest amount on the loan, the transferor and transferee shall share in the principal and interest payments on the basis of their proportionate ownership interest in the loan. In contrast, if the transferor is entitled to receive an amount that represents the principal payments and the transferee is entitled to receive an amount that represents the interest payments on the loan, that arrangement would not be consistent with the participating interest definition because the transferor and transferee do not share proportionately in the cash flows received from the loan. In other cases, a transferor may transfer a portion of an individual loan that represents either a senior interest or a junior interest in an individual loan. In both of those cases, the transferor would account for the transfer as a secured borrowing because the senior interest or junior interest in the loan do not meet the requirements to be participating interests (see paragraph 26H).

26E. Paragraph 8B(b) states that cash flows allocated as compensation for services performed, if any, shall not be included in that determination provided that those cash flows are not subordinate to the proportionate cash flows of the participating interest and are not significantly above an amount that would fairly compensate a substitute service provider, should one be required, including any profit that would be demanded in the marketplace. Cash flows allocated as compensation for services performed that are significantly above an amount that would fairly compensate a substitute service provider would result in a disproportionate division of cash flows of the entire financial asset among the participating interest holders and, therefore, would preclude the portion of a transferred financial asset from meeting the definition of a participating interest. Examples of cash flows that are compensation for services performed include loan origination fees (as defined by FASB Statement No. 91, *Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases*) paid by the borrower to the transferor, fees necessary to arrange and complete the transfer paid by the transferee to the transferor, and fees for servicing the financial asset.

26F. The transfer of a portion of an entire financial asset may result in a gain or loss on the transfer when the contractual interest rate on the entire financial asset differs from the market rate at the time of transfer. Paragraph 8B(b) states that any cash flows received by the transferor as proceeds of a transfer of a participating interest shall be excluded from the determination of whether the cash flows of the participating interest are proportionate provided that the transfer does not result in the transferor receiving an ownership interest in the financial asset that permits it to receive disproportionate cash flows. For example, if the transferor transfers an interest in an entire financial asset and the transferee agrees to incorporate the excess interest (between the contractual interest rate on the financial asset and the market interest rate at the date of transfer) into the contractually specified servicing fee, the excess interest would likely result in the conveyance of an interest-only strip to the transferor from the transferee. An interest-only strip would result in a disproportionate division of cash flows of the financial asset among the participating interest holders and would preclude the portion from meeting the definition of a participating interest.

26G. Paragraph 8B(c) requires that the rights of each participating interest holder (including the transferor in its role as participating interest holder) have the same priority and that no participating interest holder's interest is subordinated to the interest of another participating interest holder. In certain transfers, recourse is provided to the transferee that requires the transferor to reimburse any premium paid by the transferee if the underlying financial asset is prepaid within a defined timeframe of the transfer date. Such recourse would preclude the transferred portion from meeting the definition of a participating interest. However, once the recourse provision expires, the transferred portion shall be reevaluated to determine if it meets the participating interest definition.

26H. Paragraph 8B(c) also requires that participating interest holders have no recourse to the transferor (or its consolidated affiliates included in the financial statements being presented or its agents) or to each other, other than standard representations and warranties, ongoing contractual obligations to service the entire financial asset and administer the transfer contract, and contractual obligations to share in any setoff benefits. Recourse in the form of an independent third-party guarantee shall be excluded from the evaluation of whether the participating interest definition is met. Similarly, cash flows allocated to a third-party guarantor for the guarantee fee shall be excluded from the determination of whether the cash flows are divided proportionately among the participating interest holders.

Isolation beyond the Reach of the Transferor and Its Creditors

27. The nature and extent of supporting evidence required for an assertion in financial statements that an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset (which are referred to collectively in this Statement as *transferred financial assets*) ~~transferred financial assets~~ have been isolated—put presumptively beyond the reach of the transferor, any of its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial

statements being presented, and its creditors, either by a single transaction or a series of transactions taken as a whole—depend on the facts and circumstances. All available evidence that either supports or questions an assertion shall be considered, including~~.~~ ~~That consideration includes making judgments about~~ whether the contract or circumstances permit the transferor to revoke the transfer. It also may include ~~making judgments about the kind of~~ consideration of the legal consequences of the transfer in the jurisdiction in which bankruptcy or other receivership would take place~~into which a transferor or SPE might be placed~~, whether a transfer of financial assets would likely be deemed a true sale at law (as described in paragraph 27A) or otherwise isolated (as described in paragraph 27B), whether the transferor is affiliated with the transferee, and other factors pertinent under applicable law. Derecognition of transferred financial assets is appropriate only if the available evidence provides reasonable assurance that the transferred financial assets would be beyond the reach of the powers of a bankruptcy trustee or other receiver for the transferor or any of its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented and its creditors ~~**consolidated affiliate of the transferor** that is not a special-purpose corporation or other entity designed to make remote the possibility that it would enter bankruptcy or other receivership~~ (paragraph 83(c)).

27A. In the context of U.S. bankruptcy laws, a true sale opinion from an attorney is often required to support a conclusion that transferred financial assets are isolated from the transferor, and any of its consolidated affiliates included in the financial statements being presented, and its creditors. In addition, a nonconsolidation opinion is often required if the transfer is to an affiliated entity. In the context of U.S. bankruptcy laws:

a. A true sale opinion is an attorney's conclusion that the transferred financial assets have been sold and are beyond the reach of the transferor's creditors and that a court would conclude that the transferred financial assets would not be included in the transferor's bankruptcy estate.
b. A nonconsolidation opinion is an attorney's conclusion that a court would recognize that an entity holding the transferred financial assets exists separately from the transferor. Additionally, a nonconsolidation opinion is an attorney's conclusion that a court would not order the substantive consolidation of the assets and liabilities of the entity holding the transferred financial assets and the assets and liabilities of the transferor (and its consolidated affiliates included in the financial statements being presented) in the event of the transferor's bankruptcy or receivership.

A legal opinion may not be required if a transferor has a reasonable basis to conclude that the appropriate legal opinion(s) would be given if requested. For example, the transferor might reach a conclusion without consulting an attorney if (1) the transfer is a routine transfer of financial assets that does not result in any continuing involvement by the transferor or (2) the transferor had experience with other transfers with similar facts and circumstances under the same applicable laws and regulations.

27B. For entities that are subject to other possible bankruptcy, conservatorship, or other receivership procedures (for example, banks subject to receivership by the Federal Deposit Insurance Corporation [FDIC]) in the United States or other jurisdictions, judgments about whether transferred financial assets have been isolated need to be made in relation to the powers of bankruptcy courts or trustees, conservators, or receivers in those jurisdictions.

28. Whether securitizations isolate transferred financial assets may depend on such factors as whether the securitization is accomplished in one step or multiple ~~two~~ steps transfers (paragraphs 80–84). Some ~~Many~~ common financial transactions, for example, typical repurchase agreements and securities lending transactions, may isolate transferred financial assets from the transferor, although they may not meet the other ~~criteria~~ conditions for surrender of control (paragraph 9).

Conditions That Constrain a Transferee

29. Sale accounting is allowed under paragraph 9(b) only if each transferee (or, if the transferee is an entity whose sole purpose is to engage in securitization or asset-backed financing arrangements and that entity is constrained from pledging or exchanging the assets it receives, each third-party holder of its beneficial interests) has the right to pledge~~,~~ or ~~the right to~~ exchange~~,~~ the ~~transferred~~ assets or beneficial interests it received, ~~but constraints on that right also matter~~ and no condition both constrains the transferee (or third-party holder of its beneficial interests) from taking advantage of its right to pledge or exchange and provides more than a trivial benefit to the transferor. Many transferor-imposed or other conditions on a

transferee's right to pledge or exchange ~~a transferred asset~~ both constrain a transferee from pledging or exchanging ~~the transferred assets~~ and, through that constraint, provide more than a trivial benefit to the transferor. Judgment is required to assess whether a particular condition results in a constraint. Judgment also is required to assess whether a constraint provides a more-than-trivial benefit to the transferor. If the transferee is an entity whose sole purpose is to engage in securitization or asset-backed financing activities, that entity may be constrained from pledging or exchanging the transferred financial assets to protect the rights of beneficial interest holders in the financial assets of the entity. Paragraph 9(b) requires that the transferor look through the constrained entity to determine whether each third-party holder of its beneficial interests has the right to pledge or exchange the beneficial interests that it holds. The considerations in paragraphs 29A–32 apply to the transferee or the third-party holders of its beneficial interests in an entity that is constrained from pledging or exchanging the assets it receives and whose sole purpose is to engage in securitization or asset-backed financing activities. ~~For example, a provision in the transfer contract that prohibits selling or pledging a transferred loan receivable not only constrains the transferee but also provides the transferor with the more-than-trivial benefits of knowing who has the asset, a prerequisite to repurchasing the asset, and of being able to block the asset from finding its way into the hands of a competitor for the loan customer's business or someone that the loan customer might consider an undesirable creditor. Transferor-imposed contractual constraints that narrowly limit timing or terms, for example, allowing a transferee to pledge only on the day assets are obtained or only on terms agreed with the transferor, also constrain the transferee and presumptively provide the transferor with more-than-trivial benefits.~~

29A. Some conditions may constrain a transferee from pledging or exchanging the financial asset and may provide the transferor with more than a trivial benefit. For example, a provision that prohibits selling or pledging a transferred loan receivable not only constrains the transferee but also provides the transferor with the more-than-trivial benefit of knowing who holds the financial asset (a prerequisite to repurchasing the financial asset) and of being able to block the financial asset from being transferred to a competitor for the loan customer's business. Transferor-imposed contractual constraints that narrowly limit timing or terms, for example, allowing a transferee to pledge only on the day assets are obtained or only on terms agreed to with the transferor, also constrain the transferee and presumptively provide the transferor with more-than-trivial benefits. In some circumstances in which the transferor has no continuing involvement with the transferred financial assets, some conditions may constrain a transferee from pledging or exchanging the financial assets. If the transferor, its consolidated affiliates included in the financial statements being presented, and its agents have no continuing involvement with the transferred financial assets, the condition under paragraph 9(b) is met. For example, if a transferor receives only cash in return for the transferred financial assets and the transferor, its consolidated affiliates included in the financial statements being presented, and its agents have no continuing involvement with the transferred financial assets, sale accounting is allowed under paragraph 9(b) even if the transferee entity is significantly limited in its ability to pledge or exchange the transferred assets.

30. However, some conditions may ~~do~~ not constrain a transferee from pledging or exchanging the transferred financial asset ~~and therefore do not preclude a transfer subject to such a condition from being accounted for as a sale~~. For example, a transferor's right of first refusal on the occurrence of a bona fide offer to the transferee from a third party presumptively would not constrain a transferee~~,~~. This is because ~~that~~ the right in itself does not enable the transferor to compel the transferee to sell the ~~assets~~ financial asset and the transferee would be in a position to receive the sum offered by exchanging the financial asset, albeit possibly from the transferor rather than the third party. Further examples of conditions that presumptively would not constrain a transferee for purposes of this Statement include (a) a requirement to obtain the transferor's permission to sell or pledge that is not to be unreasonably withheld, (b) a prohibition on sale to the transferor's competitor if other potential willing buyers exist, (c) a regulatory limitation such as on the number or nature of eligible transferees (as in the case of securities issued under Securities Act Rule 144A or debt placed privately), and (d) illiquidity, for example, the absence of an active market. ~~Judgment~~ However, judgment is required to assess the significance of some conditions. For example, a prohibition on sale to the transferor's competitor would be a ~~significant~~ constraint if that competitor were the only potential willing buyer other than the transferor.

31. A condition imposed by a transferor that constrains the transferee presumptively provides more

than a trivial benefit to the transferor. A condition *not* imposed by the transferor that constrains the transferee may or may not provide more than a trivial benefit to the transferor. For example, if the transferor refrains from imposing its usual contractual constraint on a specific transfer because it knows an equivalent constraint is already imposed on the transferee by a third party, it presumptively benefits more than trivially from that constraint. However, the transferor cannot benefit from a constraint if it is unaware at the time of the transfer that the transferee is constrained.

Transferor's Rights or Obligations to Reacquire Transferred Assets or Beneficial Interests

32. Some rights or obligations to reacquire transferred financial assets or beneficial interests both constrain the transferee and provide more than a trivial benefit to the transferor, thus precluding sale accounting under paragraph 9(b). ~~For example, a~~ A **freestanding call** option written by a transferee to the transferor ~~benefits~~ may benefit the transferor and, if the transferred financial assets are not readily obtainable in the marketplace, is likely to constrain a transferee because ~~it~~ the transferee might have to default if the call was exercised and ~~it~~ the transferee had ~~exchanged or~~ pledged or exchanged the financial assets. For example, if a transferor in a securitization transaction has a call option to repurchase third-party beneficial interests at the price paid plus a stated return, that arrangement conveys more than a trivial benefit to the transferor (paragraphs 50 and 51). If the third-party holders of its beneficial interests are constrained from pledging or exchanging their beneficial interests due to that call option, the transferor would be precluded from accounting for the transfer of financial assets to the securitization entity as a sale. ~~A~~ Similarly, a freestanding forward purchase-sale contract between the transferor and the transferee on transferred financial assets not readily obtainable in the marketplace would benefit the transferor and is likely to constrain a transferee in much the same manner. ~~Judgment is necessary to assess constraint and benefit. For example, put options written to the transferee generally do not constrain it, but a put option on a not-readily-obtainable asset may benefit the transferor and effectively constrain the transferee if the option is sufficiently deep-in-the-money when it is written that it is probable that the transferee will exercise it and the transferor will reacquire the transferred asset. In contrast, a sufficiently out-of-the-money call option held by the transferor may not constrain a transferee if it is probable when the option is written that it will not be exercised. Freestanding~~ Alternatively, freestanding rights to reacquire transferred assets that are readily obtainable presumptively do not constrain the transferee from ~~exchanging or~~ pledging or exchanging them and thus do not preclude sale accounting under paragraph 9(b).

33. Other rights or obligations to reacquire transferred financial assets, regardless of whether they constrain the transferee, may result in the transferor's maintaining effective control over the transferred financial assets, as discussed in paragraphs 46A~~50~~–54A, thus precluding sale accounting under paragraph 9(c)~~(2)~~.~~[15]~~ For example, an **attached call** in itself would not constrain a transferee who is able, by exchanging or pledging the asset subject to that call, to obtain substantially all of its economic benefits. However, an attached call could result in the transferor's maintaining effective control over the transferred asset(s) because the attached call gives the transferor the unilateral ability to cause whoever holds that specific asset to return it.

~~***Conditions That Constrain a Holder of Beneficial Interests in a Qualifying SPE***~~

~~34. The considerations in paragraphs 29–32, about conditions that may or may not constrain a transferee that is not a qualifying SPE from pledging or exchanging the transferred assets, also extend to conditions that may or may not constrain a BIH from pledging or exchanging its beneficial interests in assets transferred to a qualifying SPE. For example, if BIHs agree to sell their beneficial interests in a qualifying SPE back to the transferor upon request at the price paid plus a stated return, that arrangement clearly conveys more than a trivial benefit to the transferor; sale accounting for the transfer to the qualifying SPE would be precluded if that agreement constrained a BIH from exchanging or pledging its beneficial interest.~~

~~[15]And it is necessary to consider the overall effect of related rights and obligations in assessing such matters as whether a transferee is constrained or a transferor has maintained effective control. For example, if the transferor or its affiliate or agent is the servicer for the transferred asset and is empowered to decide to put the asset up for sale, and has the right of first refusal, that combination would place the transferor in position to unilaterally cause the return of a specific transferred asset and thus maintain the transferor's effective control of the transferred asset as discussed in paragraphs 9(c)(2) and 50.~~

~~**Qualifying SPE**~~

~~35. A qualifying SPE[16] is a trust or other legal vehicle that meets *all* of the following conditions:~~

~~a. It is demonstrably distinct from the transferor (paragraph 36).~~
~~b. Its permitted activities (1) are significantly limited, (2) were entirely specified in the legal documents that established the SPE or created the beneficial interests in the transferred assets that it holds, and (3) may be significantly changed only with the approval of the holders of at least a majority of the beneficial interests held by entities other than any transferor, its affiliates, and its agents (paragraphs 37 and 38).~~
~~c. It may hold only:~~
   ~~(1) Financial assets transferred to it that are passive in nature (paragraph 39)~~
   ~~(2) Passive **derivative financial instruments** that pertain to beneficial interests issued or sold to parties other than the transferor, its affiliates, or its agents (paragraphs 39 and 40)~~
   ~~(3) Financial assets (for example, guarantees or rights to collateral) that would reimburse it if others were to fail to adequately service financial assets transferred to it or to timely pay obligations due to it and that it entered into when it was established, when assets were transferred to it, or when beneficial interests (other than derivative financial instruments) were issued by the SPE~~
   ~~(4) Servicing rights related to financial assets that it holds~~
   ~~(5) Temporarily, nonfinancial assets obtained in connection with the collection of financial assets that it holds (paragraph 41)~~
   ~~(6) Cash collected from assets that it holds and investments purchased with that cash pending distribution to holders of beneficial interests that are appropriate for that purpose (that is, money-market or other relatively risk-free instruments without options and with maturities no later than the expected distribution date).~~
~~d. If it can sell or otherwise dispose of noncash financial assets, it can do so only in automatic response to one of the following conditions:~~
   ~~(1) Occurrence of an event or circumstance that (a) is specified in the legal documents that established the SPE or created the beneficial interests in the transferred assets that it holds; (b) is outside the control of the transferor, its affiliates, or its agents; and (c) causes, or is expected at the date of transfer to cause, the fair value of those financial assets to decline by a specified degree below the fair value of those assets when the SPE obtained them (paragraphs 42 and 43)~~
   ~~(2) Exercise by a BIH (other than the transferor, its affiliates, or its agents) of a right to put that holder's beneficial interest back to the SPE (paragraph 44)~~
   ~~(3) Exercise by the transferor of a call or ROAP specified in the legal documents that established the SPE, transferred assets to the SPE, or created the beneficial interests in the transferred assets that it holds (paragraphs 51–54 and 85–88)~~
   ~~(4) Termination of the SPE or maturity of the beneficial interests in those financial assets on a fixed or determinable date that is specified at inception (paragraph 45).~~

~~***Need to Be Demonstrably Distinct from the Transferor***~~

~~36. A qualifying SPE is demonstrably distinct from the transferor only if it cannot be unilaterally dissolved by any transferor, its affiliates, or its agents and either (a) at least 10 percent of the fair value of its beneficial interests is held by parties other than any transferor, its affiliates, or its agents or (b) the transfer is a guaranteed mortgage securitization.[17] An ability to unilaterally dissolve an SPE can take many forms, including but not limited to holding sufficient beneficial interests to demand that the trustee dissolve the SPE, the right to call all the assets transferred to the SPE, and a right to call or a prepayment privilege on the beneficial interests held by other parties.~~

~~[16]The description of a qualifying SPE is restrictive. The accounting for qualifying SPEs and transfers of financial assets to them should not be extended to any entity that does not currently satisfy all of the conditions articulated in this paragraph.~~

~~[17]In effect of that provision, in conjunction with paragraph 46, is that mortgage-backed securities that continue to be held by a transferor in a guaranteed mortgage securitization in which the SPE meets all conditions for being a qualifying SPE are classified in the financial statements of the transferor as securities that are subsequently measured under Statement 115.~~

~~*Limits on Permitted Activities*~~

~~37. The powers of the SPE must be limited to those activities allowed by paragraph 35 for it to be a qualifying SPE. Many kinds of entities are not so limited. For example, any bank, insurance company, pension plan, or investment company has powers that cannot be sufficiently limited for it to be a qualifying SPE.~~

~~38. The BIHs other than any transferor, its affiliates, or its agents may have the ability to change the powers of a qualifying SPE. If the powers of a previously qualifying SPE are changed so that the SPE is no longer qualifying, unless the conditions in paragraph 9(b) are then met by the SPE itself and the conditions in paragraphs 9(a) and 9(c) continue to be met, that change would bring the transferred assets held in the SPE back under the control of the transferor (paragraph 55).~~

~~*Limits on What a Qualifying SPE May Hold*~~

~~39. A financial asset or derivative financial instrument is passive only if holding the asset or instrument does not involve its holder in making decisions other than the decisions inherent in servicing (paragraph 61). An equity instrument is not passive if the qualifying SPE can exercise the voting rights and is permitted to choose how to vote. Investments are not passive if through them, either in themselves or in combination with other investments or rights, the SPE or any related entity, such as the transferor, its affiliates, or its agents, is able to exercise control or significant influence (as defined in generally accepted accounting principles for consolidation policy and for the equity method, respectively) over the investee. A derivative financial instrument is not passive if, for example, it includes an option allowing the SPE to choose to call or put other financial instruments; but other derivative financial instruments can be passive, for example, interest rate caps and swaps and forward contracts. Derivative financial instruments that result in liabilities, like other liabilities of a qualifying SPE, are a kind of beneficial interest in the qualifying SPE's assets.~~

~~40. A derivative financial instrument pertains to beneficial interests issued only if it:~~

a. ~~Is entered into (1) when the beneficial interests are issued by the qualifying SPE to parties other than the transferor, its affiliates, or its agents or sold to such other parties after being issued by the qualifying SPE to the transferor, its affiliates, or its agents or (2) when a passive derivative financial instrument needs to be replaced upon occurrence of an event or circumstance (specified in the legal documents that established the SPE or created the beneficial interests in the transferred assets that it holds) outside the control of the transferor, its affiliates, or its agents, for example, when the counterparty to the derivative defaults or is downgraded below a specified threshold~~
b. ~~Has a notional amount that does not initially exceed the amount of those beneficial interests and is not expected to exceed them subsequently~~
c. ~~Has characteristics that relate to, and partly or fully but not excessively counteract, some risk associated with those beneficial interests or the related transferred assets.~~

~~41. A qualifying SPE may hold nonfinancial assets other than servicing rights only temporarily and only if those nonfinancial assets result from collecting the transferred financial assets. For example, a qualifying SPE could be permitted to temporarily hold foreclosed nonfinancial collateral. In contrast, an entity cannot be a qualifying SPE if, for example, it receives from a transferor significant secured financial assets likely to default with the expectation that it will foreclose on and profitably manage the securing nonfinancial assets. A qualifying SPE also may hold the residual value of a sales-type or a direct financing lease only to the extent that it is guaranteed at the inception of the lease either by the lessee or by a third party financially capable of discharging the obligations that may arise from the guarantee (paragraph 89).~~

~~*Limits on Sales or Other Dispositions of Assets*~~

~~42. Examples of requirements to sell, exchange, put, or distribute (hereinafter referred to collectively as dispose of) noncash financial assets that *are* permitted activities of a qualifying SPE—because they respond automatically to the occurrence of an event or circumstance that (a) is specified in the legal documents that established the SPE or created the beneficial interests in the transferred assets that it holds; (b) is outside the control of the transferor, its affiliates, or its agents; and (c) causes, or is expected to cause, the fair value of those assets to decline by a specified degree below the fair value of those assets when the qualifying SPE obtained them—include requirements to dispose of transferred assets in response to:~~

a. ~~A failure to properly service transferred assets that could result in the loss of a substantial third-party credit guarantee~~

~~b. A default by the obligor~~

~~c. A downgrade by a major rating agency of the transferred assets or of the underlying obligor to a rating below a specified minimum rating~~

~~d. The involuntary insolvency of the transferor~~

~~e. A decline in the fair value of the transferred assets to a specified value less than their fair value at the time they were transferred to the SPE.~~

~~43. The following are examples of powers or requirements to dispose of noncash financial assets that *are not* permitted activities of a qualifying SPE, because they do not respond automatically to the occurrence of a specified event or circumstance outside the control of the transferor, its affiliates, or its agents that causes, or is expected to cause, the fair value of those transferred assets to decline by a specified degree below the fair value of those assets when the SPE obtained them:~~

~~a. A power that allows an SPE to choose to either dispose of transferred assets or hold them in response to a default, a downgrade, a decline in fair value, or a servicing failure~~

~~b. A requirement to dispose of marketable equity securities upon a specified decline from their "highest fair value" if that power could result in disposing of the asset in exchange for an amount that is more than the fair value of those assets at the time they were transferred to the SPE~~

~~c. A requirement to dispose of transferred assets in response to the violation of a nonsubstantive contractual provision (that is, a provision for which there is not a sufficiently large disincentive to ensure performance).~~

~~44. A qualifying SPE may dispose of transferred assets automatically to the extent necessary to comply with the exercise by a BIH (other than the transferor, its affiliates, or its agents) of its right to put beneficial interests back to the SPE in exchange for:~~

~~a. A full or partial distribution of those assets~~

~~b. Cash (which may require that the SPE dispose of those assets or issue beneficial interests to generate cash to fund settlement of the put)~~

~~c. New beneficial interests in those assets.~~

~~45. A qualifying SPE may have the power to dispose of assets to a party other than the transferor, its affiliate, or its agent on termination of the SPE or maturity of the beneficial interests, but only automatically on fixed or determinable dates that are specified at inception. For example, if an SPE is required to dispose of long-term mortgage loans and terminate itself at the earlier of (a) the specified maturity of beneficial interests in those mortgage loans or (b) the date of prepayment of a specified amount of the transferred mortgage loans, the termination date is a fixed or determinable date that was specified at inception. In contrast, if that SPE has the power to dispose of transferred assets on two specified dates and the SPE can decide which transferred assets to sell on each date, the termination date is *not* a fixed or determinable date that was specified at inception.~~

~~*Qualifying SPEs and Consolidated Financial Statements*~~

~~46. A qualifying SPE shall not be consolidated in the financial statements of a transferor or its affiliates.~~

~~Maintaining~~ Effective Control over Transferred Financial Assets or Beneficial Interests

46A. Judgment is required to assess whether the transferor maintains effective control over transferred financial assets or third-party beneficial interests. The transferor must evaluate whether a combination of multiple arrangements maintains effective control of transferred financial assets. When the transferee issues beneficial interests in the transferred financial assets, the evaluation of whether the transferor maintains effective control over the transferred financial assets also shall consider whether the transferor maintains effective control over the transferred financial assets through its control over the third-party beneficial interests. To assess whether the transferor maintains effective control over the transferred financial assets, all continuing involvement by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents shall be considered continuing involvement by the transferor. When assessing effective control, the transferor only considers the involvements of an agent when the agent acts for and on behalf of the transferor. In other words, if the transferor and transferee have the same agent, the agent's activities on behalf of the transferee would not be considered in the transferor's evaluation of whether it has effective control over a transferred financial asset. For example, an investment manager may act as a fiduciary (agent) for both the transferor and the transferee; therefore, the transferor need only consider the involvements of the investment manager when it is acting on its behalf.

Agreement to Repurchase or Redeem Transferred Financial Assets

47. An agreement that both entitles and obligates the transferor to repurchase or redeem transferred financial assets from the transferee maintains the transferor's effective control over those assets as described in ~~under~~ paragraph 9(c)(1)~~, and the transfer is therefore to be accounted for as a secured borrowing, if and only if~~ when all of the following conditions are met:

a. The financial assets to be repurchased or redeemed are the same or substantially the same as those transferred (paragraph 48).
b. The transferor is able to repurchase or redeem them on substantially the agreed terms, even in the event of default by the transferee (paragraph 49).
c. The agreement is to repurchase or redeem them before maturity, at a fixed or determinable price.
d. The agreement is entered into contemporaneously with, or in contemplation of, ~~concurrently with~~ the transfer.

48. To be substantially the same,[18] the financial asset that was transferred and the financial asset that is to be repurchased or redeemed need to have all of the following characteristics:

a. The same primary obligor (except for debt guaranteed by a sovereign government, central bank, government-sponsored enterprise or agency thereof, in which case the guarantor and the terms of the guarantee must be the same)
b. Identical form and type so as to provide the same risks and rights
c. The same maturity (or in the case of mortgage-backed pass-through and pay-through securities, similar remaining weighted-average maturities that result in approximately the same market yield)
d. Identical contractual interest rates
e. Similar assets as collateral
f. The same aggregate unpaid principal amount or principal amounts within accepted "good delivery" standards for the type of security involved.

49. To be able to repurchase or redeem financial assets on substantially the agreed terms, even in the event of default by the transferee, a transferor must at all times during the contract term have obtained cash or other collateral sufficient to fund substantially all of the cost of purchasing replacement financial assets from others.

Unilateral Ability to~~Ability to Unilaterally~~ Cause the Return of Specific Transferred Financial Assets

50. ~~Some rights to reacquire transferred assets (or to acquire beneficial interests in transferred assets held by a qualifying SPE), regardless of whether they constrain the transferee, may result in the transferor's maintaining effective control over the transferred assets through the **unilateral ability** to cause the return of specific transferred assets. Such rights preclude sale accounting under paragraph 9(c)(2). For example, an **attached call** in itself would not constrain a transferee who is able, by exchanging or pledging the asset subject to that call, to obtain substantially all of its economic benefits. An attached call could result, however, in the transferor's maintaining effective control over the transferred asset(s) because the attached call gives the transferor the ability to unilaterally cause whoever holds that specific asset to return it. In contrast, transfers of financial assets subject to calls embedded by the issuers of the financial instruments, for example, callable bonds or prepayable mortgage loans, do not preclude sale accounting. Such an **embedded call** does not result in the transferor's maintaining effective control, because it is the issuer rather than the transferor who holds the call.~~ A transferor maintains effective control over transferred financial assets when the transferor has the unilateral ability to cause the holder to return specific financial assets and that ability provides more than a trivial benefit to the transferor. A cleanup call, however, is permitted as an exception to that general principle. A call on a transferred financial asset provides the transferor with effective control over that financial asset if, under its price and other terms, the call provides the transferor with the unilateral ability to reclaim the transferred financial asset and conveys more than a trivial benefit to the transferor. A call or other right conveys more than a trivial benefit if the price to be paid is fixed, determinable, or otherwise potentially advantageous, unless because that price is so far out of the money or for other reasons it is probable when

[18]In this Statement, the term *substantially the same* is used consistently with the usage of that term in the AICPA Statement of Position 90-3, *Definition of the Term Substantially the Same for Holders of Debt Instruments, as Used in Certain Audit Guides and a Statement of Position.*

the option is written that the transferor will not exercise it. A transferor's unilateral ability to cause a securitization entity to return to the transferor or otherwise dispose of specific transferred financial assets, for example, in response to its decision to exit a market or a particular activity, would provide the transferor with effective control over the transferred financial assets if it provides more than a trivial benefit to the transferor. However, a call on readily obtainable assets at fair value may not provide the transferor with more than a trivial benefit. (Paragraph 53 provides an example in which, due to the combination of arrangements, the transferor would maintain effective control.)

51. Effective control over transferred financial assets can be present even if the right to reclaim is indirect. For example, if a call allows a transferor to buy back the beneficial interests at a fixed price, the transferor may maintain effective control of the financial assets underlying those beneficial interests. If the transferee is ~~a qualifying SPE, it has met the conditions in paragraph 35(d) and therefore must~~ an entity whose sole purpose is to engage in securitization or asset-backed financing activities, that entity may be constrained from choosing to ~~exchange or~~ pledge or exchange the transferred financial assets. In that circumstance, any call held by the transferor on third-party beneficial interests is effectively ~~attached to~~ an attached call on the transferred financial assets. ~~and could—depending~~ Depending on the price and other terms of the call~~—~~, the transferor may maintain ~~the transferor's~~ effective control over the transferred financial assets. ~~through the ability to unilaterally cause the transferee to return specific assets. For example, a transferor's unilateral ability to cause a qualifying SPE to return to the transferor or otherwise dispose of specific transferred assets at will or, for example, in response to its decision to exit a market or a particular activity, could provide the transferor with effective control over the transferred assets.~~

52. ~~A call that is attached to transferred assets maintains the transferor's effective control over those assets if, under its price and other terms, the call conveys more than a trivial benefit to the transferor. Similarly, any unilateral right to reclaim specific assets transferred to a qualifying SPE maintains the transferor's effective control over those assets if the right conveys more than a trivial benefit to the transferor. A call or other right conveys more than a trivial benefit if the price to be paid is fixed, determinable, or otherwise potentially advantageous, unless because that price is so far out of the money or for other reasons it is probable when the option is written that the transferor will not exercise it. Thus, for example, a call on specific assets transferred to a qualifying SPE at a price fixed at their principal amount maintains the transferor's effective control over the assets subject to that call. Effective control over transferred assets can be present even if the right to reclaim is indirect. For example, if an embedded call allows a transferor to buy back the beneficial interests of a qualifying SPE at a fixed price, then the transferor remains in effective control of the assets underlying those beneficial interests. A cleanup call, however, is permitted as an exception to that general principle.~~ An **embedded call** would not result in the transferor's maintaining effective control because it is the issuer rather than the transferor who holds the call and the call does not provide more than a trivial benefit to the transferor. For example, a call embedded by the issuer of a callable bond or the borrower of a prepayable mortgage loan would not provide the transferor with effective control over the transferred financial asset.

53. A right to reclaim specific transferred financial assets by paying their fair value when reclaimed generally does not maintain effective control~~,~~ ~~because~~ when it does not convey a more than trivial benefit to the transferor. However, a transferor has maintained effective control if it has such a right and also holds the residual interest in the transferred financial assets. For example, if a transferor holds the residual interest in securitized financial assets and can reclaim ~~such~~ the transferred financial assets at termination of the securitization entity ~~qualifying SPE~~ by purchasing them in an auction, and thus at what might appear to be fair value, then sale accounting for the transfer of those financial assets it can reclaim would be precluded. Such circumstances provide the transferor with a more than trivial benefit and effective control over the financial assets, because it can pay any price it chooses in the auction and recover any excess paid over fair value through its residual interest in the transferred financial assets.

54. ~~A transferor that has a right to reacquire transferred assets from a qualifying SPE does not maintain effective control if the reclaimed assets would be randomly selected and the amount of the assets reacquired is sufficiently limited (paragraph 87(a)), because that would not be a right to reacquire *specific* assets. Nor does~~ Some removal-of-account provisions do not result in the transferor's maintaining effective control, as discussed in paragraphs 85–88. For example, a transferor does not maintain effective

control through an obligation to reacquire transferred financial assets from a securitization entity ~~qualifying SPE~~ if the reacquisition ~~transfer~~ could occur only after a specified failure of the servicer to properly service the transferred financial assets that could result in the loss of a third-party guarantee ~~(paragraph 42(a))~~ or only after ~~a BIH other than the transferor, its affiliate, or its agent requires a qualifying SPE~~ third-party beneficial interest holders require a securitization entity to repurchase that beneficial interest ~~(paragraph 44(b))~~, because the transferor could not cause that reacquisition *unilaterally.*

Arrangements to Reacquire Transferred Financial Assets

54A. A transferor maintains effective control over the transferred financial asset as described in paragraph 9(c)(3) through an agreement that permits the transferee to require the transferor to repurchase the transferred financial asset at a price that is so favorable to the transferee at the date of the transfer that it is probable that the transferee will require the transferor to repurchase the transferred financial asset. For example, a put option written to the transferee generally does not provide the transferor with effective control over the transferred financial asset. However, a put option that is sufficiently deep in the money when it is written would provide the transferor effective control over the transferred financial asset because it is probable that the transferee will exercise the option and the transferor will be required to repurchase the transferred financial asset. In contrast, a sufficiently out-of-the-money put option held by the transferee would not provide the transferor with effective control over the transferred financial asset if it is probable when the option is written that the option will not be exercised. Likewise, a put option held by the transferee at fair value would not provide the transferor with effective control over the transferred financial asset.

Changes That Result in the Transferor's Regaining Control of Financial Assets Sold

55. A change in law~~, status of the transferee as a qualifying SPE,~~ or other circumstance may result in a transferred portion of an entire financial asset no longer meeting the conditions of a participating interest (paragraph 8B) or the transferor's regaining control of transferred financial assets after a transfer that was previously accounted for ~~appropriately~~ as a sale ~~having been sold~~, because one or more of the conditions in paragraph 9 are no longer met. Such changes~~a change~~, unless ~~it arises~~ they arise solely from ~~either~~ the initial application of this Statement, from consolidation of an entity involved in the transfer at a subsequent date (paragraph 55A), or from a change in market prices (for example, an increase in price that moves into-the-money a freestanding call on a non-readily-obtainable transferred financial asset that was originally sufficiently out-of-the-money that it was judged not to constrain the transferee), are ~~is~~ accounted for in the same manner as a purchase of the transferred financial assets from the former transferee(s) in exchange for liabilities assumed (paragraph 10 or 11). After that change, the transferor recognizes in its financial statements those transferred financial assets together with liabilities to the former transferee(s) or ~~BIHs in those assets (paragraph 38)~~ beneficial interest holders of the former transferee(s). The transferor initially measures those transferred financial assets and liabilities at fair value on the date of the change, as if the transferor purchased the transferred financial assets and assumed the liabilities on that date. The former transferee would derecognize the transferred financial assets on that date, as if it had sold the transferred financial assets in exchange for a receivable from the transferor.

55A. If a transferor subsequently consolidates an entity involved in a transfer that was accounted for as a sale, it shall account for the consolidation in accordance with applicable consolidation accounting guidance.

Measurement of Interests Held after a Transfer of Financial Assets

Assets Obtained and Liabilities Incurred as Proceeds

56. The proceeds from a sale of financial assets consist of the cash and any other assets obtained, including beneficial interests and separately recognized servicing assets, in the transfer less any liabilities incurred, including separately recognized servicing liabilities. Any asset obtained ~~that is not an interest in the transferred asset~~ is part of the proceeds from the sale. Any liability incurred, even if it is related to the transferred financial assets, is a reduction of the proceeds. Any derivative financial instrument entered into concurrently with a transfer of financial assets is either an asset obtained or a liability incurred and part of the proceeds received in the transfer. All proceeds and reductions of proceeds from a sale shall be initially measured at fair value~~, if practicable~~.

Illustration—Recording Transfers with Proceeds of Cash, Derivatives, and Other Liabilities

57. Company A transfers ~~sells~~ entire loans with a carrying amount of $1,000 to an unconsolidated securitization entity and receives proceeds with a fair value of $~~1,100~~ 1,030~~and a carrying amount of $1,000~~, and the transfer is accounted for as a sale.[18a] Company A undertakes no servicing responsibilities ~~but obtains an option to purchase from the transferee loans similar to the loans sold (which are readily obtainable in the marketplace)~~ and assumes a limited recourse obligation to repurchase delinquent loans.

Company A agrees to provide the transferee a return at a floating rate of interest even though the contractual terms of the loan are fixed rate in nature (that provision is effectively an interest rate swap).

Fair Values	
Cash proceeds	$ 1,050
Interest rate swap asset	40
~~Call option~~	~~70~~
Recourse obligation	60

Net Proceeds	
Cash received	$ 1,050
Plus: ~~Call option~~	~~70~~
Interest rate swap asset	40
Less: Recourse obligation	(60)
Net proceeds	$ 1,030~~$1,100~~

Gain on Sale	
Net proceeds	$ 1,030~~$1,100~~
Less: Carrying amount of loans sold	(1,000)
Gain on sale	$ 30~~$ 100~~

Journal Entry		
Cash	1,050	
Interest rate swap asset	40	
~~Call option~~	~~70~~	
Loans		1,000
Recourse obligation		60
Gain on sale		~~100~~30
To record transfer		

[18a]For purposes of this illustration, the transaction described in this paragraph is assumed to meet the conditions for a sale in paragraph 9 of this Statement. There is no assurance or presumption that this transaction or any other transaction in the examples in this Statement would meet the conditions in paragraph 9.

Participating Interests in Financial Assets That Continue to Be Held by a Transferor

58. ~~Other~~ Participating interests in ~~transferred~~ financial assets that continue to be held by a transferor~~—those that~~ are not part of the proceeds of the transfer~~—are interests that continue to be held by a transferor over which the transferor has not relinquished control. Interests that continue to be held by a transferor~~, and the carrying amount of those participating interests shall be measured at the date of the transfer by allocating the previous carrying amount between the participating interests transferred and ~~assets~~ sold, ~~if any,~~ and the participating interests that are not transferred and continue to be held by a transferor, based on their relative fair values.~~ Allocation procedures shall be applied to all transfers in which interests continue to be held by a transferor, even those that do not qualify as sales. Examples of interests that continue to be held by a transferor include securities backed by the transferred assets, undivided interests, and cash reserve accounts and residual interests in securitization trusts. If a transferor cannot determine whether an asset is an interest that continues to be held by a transferor or proceeds from the sale, the asset shall be treated as proceeds from the sale and accounted for in accordance with paragraph 56.~~

~~59. If the interests that continue to be held by a transferor are subordinate to more senior interests held by others, that subordination may concentrate most of the risks inherent in the transferred assets into the interests that continue to be held by a transferor and shall be taken into consideration in estimating the fair value of those interests. For example, if the amount of the gain recognized, after allocation, on a securitization with a subordinated interest that continues to be held by a transferor is greater than the gain that would have been recognized had the entire asset been sold, the transferor needs to be able to identify why that can occur. Otherwise, it is likely that the effect of subordination to a senior interest has not been adequately considered in the determination of the fair value of the subordinated interest that continues to be held by a transferor.~~

Illustration—Recording Transfers of Participating ~~Partial~~ Interests

60. Company B transfers ~~sells~~ a ~~pro rata~~ nine-tenths participating interest in a loan ~~loans~~ with a fair value of $1,100 and a carrying amount of $1,000, and the transfer is accounted for as a sale.[18b] The servicing contract has a fair value of zero ~~There is no servicing asset or liability,~~ because Company B estimates that the **benefits of servicing** are just adequate to compensate it for its servicing responsibilities.

Fair Values	
Cash proceeds for nine-tenths participating interest sold ($1,100 × 9/10)	$990
One-tenth participating interest that continues to be held by ~~a~~ the transferor ~~[($990 ÷ 9/10) × 1/10]~~ ($1,100 × 1/10)	110

[18b]See footnote 18a.

Allocated Carrying Amount Based on Relative Fair Values

	Fair Value	Percentage of Total Fair Value	Allocated Carrying Amount
Nine-tenths participating interest sold	$ 990	90	$ 900
One-tenth participating interest that continues to be held by ~~a~~ the transferor	110	10	100
Total	$ 1,100	100	$ 1,000

Gain on Sale

Net proceeds	$ 990
Less: Carrying amount of loans sold	(900)
Gain on sale	$ 90

Journal Entry

Cash	990	
Loans		900
Gain on sale		90
To record transfer		

Servicing Assets and Liabilities

61. Servicing of mortgage loans, credit card receivables, or other financial assets commonly includes, but is not limited to, collecting principal, interest, and escrow payments from borrowers; paying taxes and insurance from escrowed funds; monitoring delinquencies; executing foreclosure if necessary; temporarily investing funds pending distribution; remitting fees to guarantors, trustees, and others providing services; and accounting for and remitting principal and interest payments to the holders of beneficial interests or participating interests in the financial assets. Servicing is inherent in all financial assets; it becomes a distinct asset or liability for accounting purposes only in the circumstances described in paragraph 62. If a transferor sells a participating interest in an entire financial asset, it would recognize a servicing asset or a servicing liability only related to the participating interest sold.

62. An entity that undertakes a contract to service financial assets shall recognize either a servicing asset or a servicing liability~~;~~ each time it undertakes an obligation to service a financial asset that (a) results from a servicer's transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset ~~the servicer's financial assets~~ that meets the requirements for sale accounting~~, (b) results from a transfer of the servicer's financial assets to a qualifying SPE in a guaranteed mortgage securitization in which the transferor retains all of the resulting securities and classifies them as either available-for-sale securities or trading securities in accordance with Statement 115,~~ or (be) is acquired or assumed and the servicing obligation does not relate to financial assets of the servicer or its consolidated affiliates included in the financial statements being presented. However, if the transferor transfers the assets to an unconsolidated entity in a transfer that qualifies as a sale in which the transferor~~in a guaranteed mortgage securitization, retains all of~~ obtains the resulting securities, and classifies them as debt securities held-to-maturity in accordance with Statement 115, the servicing asset or servicing liability may be reported together with the asset being serviced and not recognized separately. A servicer of financial assets commonly receives the benefits of servicing—revenues from contractually specified

servicing fees, a portion of the interest from the financial assets, late charges, and other ancillary sources, including "float," all of which it is entitled to receive only if it performs the servicing—and incurs the costs of servicing the financial assets. Typically, the benefits of servicing are expected to be more than **adequate compensation** to a servicer for performing the servicing, and the contract results in a servicing asset. However, if the benefits of servicing are not expected to adequately compensate a servicer for performing the servicing, the contract results in a servicing liability. (A servicing asset may become a servicing liability, or vice versa, if circumstances change, and the initial measure for servicing may be zero if the benefits of servicing are just adequate to compensate the servicer for its servicing responsibilities.) A servicer would account for its servicing contract that qualifies for separate recognition as a servicing asset or a servicing liability initially measured at its fair value regardless of whether explicit consideration was exchanged.

62A. A servicer that transfers or securitizes financial assets in a transaction that does not meet the requirements for sale accounting and is accounted for as a secured borrowing with the underlying financial assets remaining on the transferor's balance sheet shall not recognize a servicing asset or a servicing liability. ~~However, if a transferor enters into a servicing contract when the transferor transfers mortgage loans in a guaranteed mortgage securitization, retains all the resulting securities, and classifies those securities as either available-for-sale securities or trading securities in accordance with Statement 115, the transferor shall separately recognize a servicing asset or a servicing liability.~~

63. A servicer that recognizes a servicing asset or servicing liability shall account for the contract to service financial assets separately from those financial assets, as follows:

a. Report servicing assets separately from servicing liabilities in the statement of financial position (paragraph 13B).
b. Initially measure servicing assets and servicing liabilities at fair value~~, if practicable~~ (paragraphs 10(c)~~, 11(b),~~ and 11(c)~~, 71, and 72~~).
c. Account separately for rights to future interest income from the serviced assets that exceed contractually specified servicing fees. Those rights are not servicing assets; they are financial assets, effectively interest-only strips to be accounted for in accordance with paragraph 14 of this Statement. (Interest-only strips preclude a portion of a financial asset from meeting the definition of a participating interest; see paragraph 26F.)
d. Identify classes of servicing assets and servicing liabilities based on (1) the availability of market inputs used in determining the fair value of servicing assets and servicing liabilities, (2) an entity's method for managing the risks of its servicing assets and servicing liabilities, or (3) both.
e. Subsequently measure each class of separately recognized servicing assets and servicing liabilities either at fair value or by amortizing the amount recognized in proportion to and over the period of estimated net servicing income for assets (the excess of servicing revenues over servicing costs) or the period of estimated net servicing loss for servicing liabilities (the excess of servicing costs over servicing revenues). Different elections can be made for different classes of servicing assets and servicing liabilities. An entity may make an irrevocable decision to subsequently measure a class of servicing assets and servicing liabilities at fair value at the beginning of any fiscal year. Once a servicing asset or a servicing liability is reported in a class of servicing assets and servicing liabilities that an entity elects to subsequently measure at fair value, that servicing asset or servicing liability cannot be placed in a class of servicing assets and servicing liabilities that is subsequently measured using the amortization method. Changes in fair value should be reported in earnings for servicing assets and servicing liabilities subsequently measured at fair value (paragraph 13A(b)).
f. Subsequently evaluate and measure impairment of each class of separately recognized servicing assets that are subsequently measured using the amortization method described in paragraph 13A(a) as follows:
   (1) Stratify servicing assets within a class based on one or more of the predominant risk characteristics of the underlying financial assets. Those characteristics may include financial asset type,[19] size, interest rate, date of origination, term, and geographic location.

[19]For example, for mortgage loans, financial asset type refers to the various conventional or government guaranteed or insured mortgage loans and adjustable-rate or fixed-rate mortgage loans.

(2) Recognize impairment through a valuation allowance for an individual stratum. The amount of impairment recognized separately shall be the amount by which the carrying amount of servicing assets for a stratum exceeds their fair value. The fair value of servicing assets that have not been recognized shall not be used in the evaluation of impairment.

(3) Adjust the valuation allowance to reflect changes in the measurement of impairment subsequent to the initial measurement of impairment. Fair value in excess of the carrying amount of servicing assets for that stratum, however, shall not be recognized. This Statement does not address when an entity should record a direct write-down of recognized servicing assets.

g. For servicing liabilities subsequently measured using the amortization method, if subsequent events have increased the fair value of the liability above the carrying amount, for example, because of significant changes in the amount or timing of actual or expected future cash flows relative to the cash flows previously projected, the servicer shall revise its earlier estimates and recognize the increased obligation as a loss in earnings (paragraph 13A).

64. As indicated above, transferors sometimes agree to take on servicing responsibilities when the future benefits of servicing are not expected to adequately compensate them for performing that servicing. In that circumstance, the result is a servicing liability rather than a servicing asset. For example, if in the transaction illustrated in paragraph 57 the transferor had agreed to service the loans without explicit compensation and it estimated the fair value of that servicing obligation at $50, net proceeds would be reduced to $980~~1,050~~, gain on sale would become ~~be reduced to $50~~a loss on sale of $20, and the transferor would report a servicing liability of $50.

Illustration—Sale of Receivables with Servicing Obtained

65. Company C originates $1,000 of loans that yield 10 percent interest income for their estimated lives of 9 years. Company C ~~sells the~~ transfers the entire loans to an unconsolidated entity and the transfer is accounted for as a sale.[19a] ~~$1,000 principal plus the right to receive interest income of 8 percent to another entity for $1,000.~~ Company C receives as proceeds $1,000 cash, a beneficial interest to receive 1 percent of the contractual interest on the loans (an interest-only strip receivable), and an additional 1 percent of the contractual interest as compensation for servicing the loans. ~~Company C will continue to service the loans, and the contract stipulates that its compensation for performing the servicing is the right to receive half of the interest income not sold. The remaining half of the interest income not sold is considered an interest-only strip receivable that Company C classifies as an available-for-sale security. At the date of the transfer, the fair value of the loans is $1,100.~~ The fair values of the servicing asset and the interest-only strip receivable are $40 and $60, respectively.

Fair Values	
Cash proceeds	$ 1,000
Servicing asset	40
Interest-only strip receivable	60

Net Proceeds	
Cash proceeds	$ 1,000
Servicing asset	40
Interest-only strip receivable	60
Net proceeds	$ 1,100~~$ 1,040~~

[19a]See footnote 18a.

~~**Carrying Amount Based on Relative Fair Values**~~

	~~Fair Value~~	~~Percentage of Total Fair Value~~	~~Allocated Carrying Amount~~
~~Loans sold~~	~~$ 1,040~~	~~94.55~~	~~$ 945.50~~
~~Interest-only strip receivable~~	~~60~~	~~5.45~~	~~54.50~~
~~Total~~	~~$ 1,100~~	~~100.00~~	~~$ 1,000.00~~

Gain on Sale	
Net proceeds	$ 1,100~~$ 1,040.00~~
Less: Carrying amount of loans sold	(1,000)~~945.50~~
Gain on sale	$ 100~~$ 94.50~~

Journal Entries		
Cash	1,000~~.00~~	
Interest-only strip receivable	60~~54.50~~	
Servicing asset	40~~.00~~	
Loans		1,000~~.00~~
Gain on sale		100~~94.50~~
To record transfer and to recognize interest-only strip receivable and servicing asset		
~~Interest-only strip receivable~~	~~5.50~~	
~~Other comprehensive income~~		~~5.50~~
~~To begin to subsequently measure interest-only strip receivable like an available-for-sale security (paragraph 14)~~		

~~66. The previous illustration demonstrates how a transferor would account for a simple sale in which servicing is obtained. Company C might instead transfer the financial assets to a corporation or a trust that is a qualifying SPE. The qualifying SPE then securitizes the loans by selling beneficial interests to the public. The qualifying SPE pays the cash proceeds to the original transferor, which accounts for the transfer as a sale and derecognizes the financial assets assuming that the criteria in paragraph 9 are met. Securitizations often combine the elements shown in paragraphs 57, 60, and 65, as illustrated below.~~

~~*Illustration—Recording Transfers of Partial Interests with Proceeds of Cash, Derivatives, Other Liabilities, and Servicing*~~

~~67. Company D originates $1,000 of prepayable loans that yield 10 percent interest income for their 9-year expected lives. Company D sells nine-tenths of the principal plus interest of 8 percent to another entity. Company D will continue to service the loans, and the contract stipulates that its compensation for performing the servicing is the 2 percent of the interest income not sold. Company D obtains an option to purchase from the transferee loans similar to the loans sold (which are readily obtainable in the marketplace) and incurs a limited recourse obligation to repurchase delinquent loans. At the date of transfer, the fair value of the loans is $1,100.~~

~~Fair Values~~	
~~Cash proceeds~~	~~$ 900~~
~~Call option~~	~~70~~
~~Recourse obligation~~	~~(60)~~
~~Servicing asset~~	~~90~~
~~One-tenth interest that continues to be held by the transferor~~	~~100~~

~~Net Proceeds~~	
~~Cash received~~	~~$ 900~~
~~Plus: Servicing asset~~	~~90~~
~~Plus: Call option~~	~~70~~
~~Less: Recourse obligation~~	~~(60)~~
~~Net proceeds~~	~~$ 1,000~~

~~Carrying Amount Based on Relative Fair Values~~

	~~Fair Value~~	~~Percentage of Total Fair Value~~	~~Allocated Carrying Amount~~
~~Interest sold~~	~~$ 1,000~~	~~90.9~~	~~$ 909~~
~~One-tenth interest that continues to be held by the transferor~~	~~100~~	~~9.1~~	~~91~~
~~Total~~	~~$ 1,100~~	~~100.0~~	~~$ 1,000~~

~~Gain on Sale~~	
~~Net proceeds~~	~~$ 1,000~~
~~Less: Carrying amount of loans sold~~	~~(909)~~
~~Gain on sale~~	~~$ 91~~

~~Loans Sold~~	
~~Carrying amount of loans~~	~~$ 1,000~~
~~Less: Allocated carrying amount of interest that continues to be held by the transferor~~	~~(91)~~
~~Loans sold~~	~~$ 909~~

~~Journal Entries~~		
~~Cash~~	~~900~~	
~~Call option~~	~~70~~	
~~Servicing asset~~	~~90~~	
~~Loans~~		~~909~~
~~Recourse obligation~~		~~60~~
~~Gain on sale~~		~~91~~
~~To record transfer and to recognize servicing asset, call option, and recourse obligation~~		

68–70. [These paragraphs have been deleted. See Status page.]

~~If It Is Not Practicable to Estimate Fair Values~~

~~71. If it is not practicable to estimate the fair values of assets, the transferor shall record those assets at zero. If it is not practicable to estimate the fair values of liabilities, the transferor shall recognize no gain on the transaction and shall record those liabilities at the greater of:~~

~~a. The excess, if any, of (1) the fair values of assets obtained less the fair values of other liabilities incurred, over (2) the sum of the carrying values of the assets transferred~~

~~b. The amount that would be recognized in accordance with FASB Statement No. 5, *Accounting for Contingencies,* as interpreted by FASB Interpretation No. 14, *Reasonable Estimation of the Amount of a Loss.*~~

~~Illustration—Recording Transfers If It Is Not Practicable to Estimate a Fair Value~~

~~72. Company E sells loans with a carrying amount of $1,000 to another entity for cash proceeds of $1,050 plus a call option to purchase loans similar to the loans sold (which are readily obtainable in the marketplace) and incurs a limited recourse obligation to repurchase any delinquent loans. Company E undertakes an obligation to service the transferred assets for the other entity. In Case 1, Company E finds it impracticable to estimate the fair value of the servicing contract, although it is confident that servicing revenues will be more than adequate compensation for performing the servicing. In Case 2, Company E finds it impracticable to estimate the fair value of the recourse obligation.~~

[20–21][These footnotes have been deleted. See Status page.]

~~**Fair Values**~~	~~**Case 1**~~	~~**Case 2**~~
~~Cash proceeds~~	~~$ 1,050~~	~~$ 1,050~~
~~Servicing asset~~	~~XX~~ *	~~40~~
~~Call option~~	~~70~~	~~70~~
~~Recourse obligation~~	~~(60)~~	~~XX~~ *
~~Fair value of loans transferred~~	~~1,100~~	~~1,100~~

~~* Not practicable to estimate fair value.~~

~~**Net Proceeds**~~	~~**Case 1**~~	~~**Case 2**~~
~~Cash received~~	~~$ 1,050~~	~~$ 1,050~~
~~Plus: Servicing asset~~	~~XX~~ *	~~40~~
~~Plus: Call option~~	~~70~~	~~70~~
~~Less: Recourse obligation~~	~~(60)~~	~~XX~~ ‡
~~Net proceeds~~	~~$ 1,060~~	~~$ 1,160~~

~~**Gain on Sale**~~	~~**Case 1**~~	~~**Case 2**~~
~~Net proceeds~~	~~$ 1,060~~	~~$ 1,160~~
~~Carrying amount of loans~~	~~1,000~~	~~1,000~~
~~Less: Recourse obligation~~	~~0~~	~~(160)~~ ‡
~~Gain on sale~~	~~$ 60~~	~~$ 0~~

~~**Journal Entries**~~	~~**Case 1**~~		~~**Case 2**~~	
~~Cash~~	~~1,050~~		~~1,050~~	
~~Servicing asset~~	~~0~~ *		~~40~~	
~~Call option~~	~~70~~		~~70~~	
~~Loans~~		~~1,000~~		~~1,000~~
~~Recourse obligation~~		~~60~~		~~160~~ ‡
~~Gain on sale~~		~~60~~		~~0~~
~~To record transfer~~				

~~* Assets shall be recorded at zero if an estimate of the fair value of the assets is not practicable.~~

~~‡ The amount recorded as a liability in this example equals the sum of the known assets less the fair value of the known liabilities, that is, the amount that results in no gain or loss.~~

Securitizations

73. Financial assets such as mortgage loans, automobile loans, trade receivables, credit card receivables, and other revolving charge accounts are financial assets commonly transferred in securitizations. Securitizations of mortgage loans may include pools of single-family residential mortgages or other types of real estate mortgage loans, for example, multifamily residential mortgages and commercial property mortgages. Securitizations of loans secured by chattel mortgages on automotive vehicles as well as other equipment (including direct financing or sales-type leases) also are common. Both financial and nonfinancial assets can be securitized; life insurance policy loans, patent and copyright royalties, and even taxi medallions also have been securitized. But securitizations of nonfinancial assets are outside the scope of this Statement.

74. An originator of a typical securitization (the transferor) transfers a portfolio of financial assets to a securitization entity ~~an SPE~~, commonly a trust. In "pass-through" and "pay-through" securitizations, receivables are transferred to the ~~SPE~~ entity at the inception of the securitization, and no further transfers are made; all cash collections are paid to the holders of beneficial interests in the entity ~~SPE~~. In "revolv-

ing-period" securitizations, receivables are transferred at the inception and also periodically (daily or monthly) thereafter for a defined period (commonly three to eight years), referred to as the revolving period. During the revolving period, the ~~SPE~~ entity uses most of the cash collections to purchase additional receivables from the transferor on prearranged terms.

75. Beneficial interests in the securitization entity ~~SPE~~ are sold to investors and the proceeds are used to pay the transferor for the ~~assets~~ transferred financial assets. Those beneficial interests may comprise either a single class having equity characteristics or multiple classes of interests, some having debt characteristics and others having equity characteristics. The cash collected from the portfolio is distributed to the investors and others as specified by the legal documents that established the entity ~~SPE~~.

76. Pass-through, pay-through, and revolving-period securitizations that meet the ~~criteria~~ conditions in paragraph 9 qualify for sale accounting under this Statement, provided that the securitization entity is not consolidated by the transferor or its consolidated affiliates in the financial statements being presented. All financial assets obtained ~~or that continue to be held by a transferor~~ and liabilities incurred by the transferor ~~originator~~ of a securitization that qualifies as a sale shall be recognized and measured as provided in paragraphs 10 and 11; that includes the implicit forward contract to sell additional financial assets ~~new receivables~~ during a revolving period, which may become valuable or onerous to the transferor as interest rates and other market conditions change.

Revolving-Period Securitizations

77. The value of the forward contract implicit in a revolving-period securitization arises from the difference between the agreed-upon rate of return to investors on their beneficial interests in the trust and current market rates of return on similar investments. For example, if the agreed-upon annual rate of return to investors in a trust is 6 percent, and later market rates of return for those investments increased to 7 percent, the forward contract's value to the transferor (and burden to the investors) would approximate the present value of 1 percent of the amount of the investment for each year remaining in the revolving structure after the receivables already transferred have been collected. If a forward contract to sell receivables is entered into at the market rate, its value at inception may be zero. Changes in the fair value of the forward contract are likely to be greater if the investors receive a fixed rate than if the investors receive a rate that varies based on changes in market rates.

78. Gain or loss recognition for revolving-period receivables sold to a securitization trust is limited to receivables that exist and have been sold. Recognition of servicing assets or servicing liabilities for revolving-period receivables is similarly limited to the servicing for the receivables that exist and have been sold~~transferred~~. As new receivables are sold, rights to service them may become assets or liabilities that ~~and~~ are recognized.

~~79. Revolving-period securitizations may use either a discrete trust, used for a single securitization, or a master trust, used for many securitizations. To achieve another securitization using an existing master trust, a transferor first transfers additional receivables to the trust and then sells additional ownership interests in the trust to investors. Adding receivables to a master trust, in itself, is neither a sale nor a secured borrowing under paragraph 9, because that transfer only increases the transferor's beneficial interest in the trust's assets. A sale or secured borrowing does not occur until the transferor receives consideration other than beneficial interests in the transferred assets. Transfers that result in an exchange of cash, that is, either transfers that in essence replace previously transferred receivables that have been collected or sales of beneficial interests to outside investors, are transfers in exchange for consideration other than beneficial interests in the transferred assets and thus are accounted for as sales (if they satisfy all the criteria in paragraph 9) or as secured borrowings.~~

Isolation of Transferred Financial Assets in Securitizations

80. A securitization carried out in one transfer or a series of transfers may or may not isolate the transferred financial assets beyond the reach of the transferor, its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented, and its creditors. Whether it does depends on the structure of the securitization transaction taken as a whole, considering such factors as the type and extent of further involvement in arrangements to protect investors from credit, ~~and~~ interest rate, and other risks, the availability of other financial assets, and the

powers of bankruptcy courts or other receivers. The discussion in paragraphs 81–83 relates only to the isolation condition in paragraph 9(a). The conditions in paragraphs 9(b) and 9(c) also must be considered to determine whether a transferor has surrendered control over the transferred financial assets.

81. In certain securitizations, a corporation that, if it failed, would be subject to the U.S. Bankruptcy Code transfers financial assets to a securitization entity ~~special-purpose trust~~ in exchange for cash. The entity ~~trust~~ raises that cash by issuing to investors beneficial interests that pass through all cash received from the financial assets, and the transferor has no further involvement with the trust or the transferred financial assets. The Board understands that those securitizations generally would be judged as having isolated the assets~~;~~, because, in the absence of any continuing involvement, there would be reasonable assurance that the transfer would be found to be a true sale at law that places the assets beyond the reach of the transferor, its consolidated affiliates (that are not entities designed to make remote the possibility that it would enter bankruptcy or other receivership) included in the financial statements being presented, and its creditors, even in bankruptcy or other receivership.

82. In other securitizations, a similar corporation transfers financial assets to a securitization entity ~~an SPE~~ in exchange for cash and beneficial interests in the transferred financial assets. That entity raises the cash by issuing to investors commercial paper that gives them a senior beneficial interest in cash received from the financial assets. The beneficial interests obtained ~~that continue to be held~~ by the transferring corporation represent a junior interest to be reduced by any credit losses on the financial assets in the entity~~trust~~. The senior beneficial ~~commercial paper~~ interests (commercial paper) are highly rated by credit rating agencies only if both (a) the credit enhancement from the junior interest is sufficient and (b) the transferor is highly rated. Depending on facts and circumstances, the Board understands that those "single-step" securitizations often would be judged in the United States as not having isolated the financial assets, because the nature of the continuing involvement may make it difficult to obtain reasonable assurance that the transfer would be found to be a true sale at law that places the financial assets beyond the reach of the transferor, its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements presented, and its creditors in U.S. bankruptcy (paragraph 113). If the transferor fell into bankruptcy and the transfer was found not to be a true sale at law, investors in the transferred financial assets might be subjected to an automatic stay that would delay payments due them, and they might have to share in bankruptcy expenses and suffer further losses if the transfer was recharacterized as a secured loan.

83. Still other securitizations use multiple ~~two~~ transfers intended to isolate transferred financial assets beyond the reach of the transferor, its consolidated affiliates (that are not entities designed to make remote the possibility that it would enter bankruptcy or other receivership) included in the financial statements presented, and its creditors, even in bankruptcy. For example, in ~~In those~~ "two-step" structures:

a. First, the corporation transfers a group of financial assets to a special-purpose corporation that, although wholly owned, is so designed that the possibility is remote that the transferor, its other consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented, or its creditors could reclaim the financial assets ~~is remote~~. This first transfer is designed to be judged to be a true sale at law, in part because the transferor does not provide "excessive" credit or yield protection to the special-purpose corporation, and the Board understands that transferred financial assets are likely to be judged beyond the reach of the transferor, its other consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented, or the transferor's creditors even in bankruptcy or other receivership.
b. Second, the special-purpose corporation transfers ~~the assets~~ a group of financial assets to a trust or other legal vehicle with a sufficient increase in the credit or yield protection on the second transfer (provided by a transferor's junior beneficial interest ~~that continues to be held by the transferor~~ or other means) to merit the high credit rating sought by third-party investors who buy senior beneficial interests in the trust. Because of that aspect of its design, that second transfer might not be judged to be a true sale at law and, thus, the transferred financial assets could at least in theory be reached by a bankruptcy trustee for the special-purpose corporation.

c. However, the special-purpose corporation is designed to make remote the possibility that it would enter bankruptcy, either by itself or by substantive consolidation into a bankruptcy of its parent should that occur. For example, its charter forbids it from undertaking any other business or incurring any liabilities, so that there can be no creditors to petition to place it in bankruptcy. Furthermore, its dedication to a single purpose is intended to make it extremely unlikely, even if it somehow entered bankruptcy, that a receiver under the U.S. Bankruptcy Code could reclaim the transferred financial assets because it has no other assets to substitute for the transferred financial assets.

The Board understands that the "two-step" securitizations described above, taken as a whole, generally would be judged under present U.S. law as having isolated the financial assets beyond the reach of the transferor, its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements presented, and its creditors, even in bankruptcy or other receivership. However, each entity involved in a transfer must be evaluated under the applicable consolidation accounting guidance. Accordingly, a transferor could be required to consolidate the trust or other legal vehicle used in the second step of the securitization, notwithstanding the isolation analysis of the transfer.

84. The powers of receivers for entities not subject to the U.S. Bankruptcy Code (for example, banks subject to receivership by the FDIC) vary considerably, and therefore some receivers may be able to reach financial assets transferred under a particular arrangement and others may not. A securitization may isolate transferred financial assets from a transferor subject to such a receiver and its creditors even though it is accomplished by only one transfer directly to a securitization entity ~~an SPE~~ that issues beneficial interests to investors and the transferor provides credit or yield protection. For entities that are subject to other possible bankruptcy, conservatorship, or other receivership procedures in the United States or other jurisdictions, judgments about whether transferred financial assets have been isolated need to be made in relation to the powers of bankruptcy courts or trustees, conservators, or receivers in those jurisdictions.

Removal-of-Accounts Provisions

85. Many transfers of financial assets that involve transfers of a group of entire financial assets to an entity whose sole purpose is to engage in securitization or asset-backed financing activities ~~in securitizations~~ empower the transferor to reclaim assets subject to certain restrictions. Such a power is sometimes called a removal-of-accounts provision (ROAP). Whether a ROAP precludes sale accounting depends on whether the ROAP results in the transferor's maintaining effective control over ~~specific~~ transferred financial assets (paragraph~~s~~ 9(c)~~(2) and 51–54~~).

86. The following are examples of ROAPs that preclude transfers from being accounted for as sales:

a. An unconditional ROAP or repurchase agreement that allows the transferor to specify the financial assets that may be removed and that provides a more-than-trivial benefit to the transferor, because such a provision allows the transferor unilaterally to remove specific financial assets
b. A ROAP conditioned on a transferor's decision to exit some portion of its business that provides a more-than-trivial benefit to the transferor, because whether it can be triggered by canceling an affinity relationship, spinning off a business segment, or accepting a third party's bid to purchase a specified (for example, geographic) portion of the transferor's business, such a provision allows the transferor unilaterally to remove specific financial assets.

87. The following are examples of ROAPs that *do not* preclude transfers from being accounted for as sales:

a. A ROAP for random removal of excess financial assets, if the ROAP is sufficiently limited so that the transferor cannot remove specific transferred financial assets, for example, by limiting removals to the amount of the transferor's interests ~~that continue to be held by the transferor~~ and to one removal per month
b. A ROAP for defaulted receivables, because the removal would be allowed only after a third party's action (default) and could not be caused unilaterally by the transferor
c. A ROAP conditioned on a third-party cancellation, or expiration without renewal, of an affinity

or private-label arrangement, because the removal would be allowed only after a third party's action (cancellation) or decision not to act (expiration) and could not be caused unilaterally by the transferor.

88. A ROAP that can be exercised only in response to a third party's action that has not yet occurred does not maintain the transferor's effective control over financial assets potentially subject to that ROAP. However, when a third party's action (such as default or cancellation) or decision not to act (expiration) occurs that allows removal of financial assets to be initiated solely by the transferor and that provides a more-than-trivial benefit to the transferor, the transferor must recognize any financial assets subject to the ROAP, whether the ROAP is exercised or not. If the ROAP is exercised, the financial assets are recognized because the transferor has reclaimed the financial assets. If the ROAP is not exercised, the financial assets subject to the ROAP are recognized because the transferor now can unilaterally cause the transferee entity ~~qualifying SPE~~ to return those specific financial assets and, therefore, the transferor once again has effective control over those transferred financial assets (paragraph 55).

Sales-Type and Direct Financing Lease Receivables

89. Sales-type and direct financing receivables secured by leased equipment, referred to as gross investment in lease receivables, are made up of two components: minimum lease payments and residual values. Minimum lease payments are requirements for lessees to pay cash to lessors and meet the definition of a financial asset. Thus, transfers of minimum lease payments are subject to the requirements of this Statement. Residual values represent the lessor's estimate of the "salvage" value of the leased equipment at the end of the lease term and may be either guaranteed or unguaranteed; residual values meet the definition of financial assets *to the extent that they are guaranteed at the inception of the lease.* Thus, transfers of residual values guaranteed at inception also are subject to the requirements of this Statement. Unguaranteed residual values do not meet the definition of financial assets, nor do residual values guaranteed after inception, and transfers of them are not subject to the requirements of this Statement. Transfers of residual values not guaranteed at inception continue to be subject to Statement 13, as amended. Because residual values guaranteed at inception are financial assets, increases to their estimated value over the life of the related lease are recognized. Entities selling or securitizing lease financing receivables shall allocate the gross investment in receivables between minimum lease payments, residual values guaranteed at inception, and residual values not guaranteed at inception using the individual carrying amounts of those components at the date of transfer. Those entities also shall record a servicing asset or servicing liability in accordance with paragraphs 10, 11, and 13, if appropriate.

Illustration—Recording Transfers of Lease Financing Receivables with Residual Values

90. At the beginning of the second year in a 10-year sales-type lease, Company F transfers ~~sells~~ for $505 a nine-tenths participating interest in the minimum lease payments to an independent third party, and the transfer is accounted for as a sale.[21a] Company F ~~and~~ retains a one-tenth participating interest in the minimum lease payments and a 100 percent interest in the unguaranteed residual value of leased equipment, which is not subject to the requirements of this Statement as discussed in paragraph 89 because it is not a financial asset and, therefore, is excluded from the analysis of whether the transfer of the nine-tenths participating interest in the minimum lease payments meets the definition of a participating interest. The servicing asset has a fair value of zero because Company F ~~receives no explicit compensation for servicing, but it~~ estimates that the ~~other~~ benefits of servicing are just adequate to compensate it for its servicing responsibilities ~~and hence initially records no servicing asset or liability~~. The carrying amounts and related gain computation are as follows:

Carrying Amounts		
Minimum lease payments		$ 540
Unearned income related to minimum lease payments		370
Gross investment in minimum lease payments		910
Unguaranteed residual value	$ 30	
Unearned income related to unguaranteed residual value	60	
Gross investment in unguaranteed residual value		90
Total gross investment in financing lease receivable		$ 1,000

Gain on Sale		
Cash received		$ 505
Nine-tenths of carrying amount of gross investment in minimum lease payments	$ 819	
Nine-tenths of carrying amount of unearned income related to minimum lease payments	333	
Net carrying amount of minimum lease payments sold		486
Gain on sale		$ 19

Journal Entry		
Cash	505	
Unearned income	333	
Lease receivable		819
Gain on sale		19
To record sale of nine-tenths of the minimum lease payments at the beginning of year 2		

[21a]See footnote 18a.

Securities Lending Transactions

91. Securities lending transactions are initiated by broker-dealers and other financial institutions that need specific securities to cover a short sale or a customer's failure to deliver securities sold. Transferees ("borrowers") of securities generally are required to provide "collateral" to the transferor ("lender") of securities, commonly cash but sometimes other securities or standby letters of credit, with a value slightly higher than that of the securities "borrowed." If the "collateral" is cash, the transferor typically earns a return by investing that cash at rates higher than the rate paid or "rebated" to the transferee. If the "collateral" is other than cash, the transferor typically receives a fee. Securities custodians or other agents commonly carry out securities lending activities on behalf of clients. Because of the protection of "collateral" (typically valued daily and adjusted frequently for changes in the market price of the securities transferred) and the short terms of the transactions, most securities lending transactions in themselves do not impose significant credit risks on either party. Other risks arise from what the parties to the transaction do with the assets they receive. For example, investments made with cash "collateral" impose market and credit risks on the transferor.

92. ~~In some securities lending transactions,~~ If the ~~criteria~~ conditions in paragraph 9 are met, ~~including the effective control criterion in paragraph 9(c), and consideration other than beneficial interests in the transferred assets is received. Those~~ securities lending transactions shall be accounted for (a) by the transferor as a sale of the "loaned" securities for proceeds consisting of the cash collateral"[22] and a forward repurchase commitment and (b) by the transferee as a purchase of the "borrowed" securities in exchange for the "collateral" and a forward resale commitment. During the term of that agreement, the transferor has surrendered control over the securities transferred and the transferee has obtained control over those securities with the ability to sell or transfer them at will. In that case, creditors of the transferor have a claim only to the "collateral" and the forward repurchase commitment.

93. However, many securities lending transactions are accompanied by an agreement that both entitles and obligates the transferor to repurchase or redeem the transferred financial assets before their maturity under which the transferor maintains effective control over those financial assets (paragraphs 47–49). Those transactions shall be accounted for as secured borrowings, in which cash (or securities that the holder is permitted by contract or custom to sell or repledge) received as "collateral" is considered the amount borrowed, the securities "loaned" are considered pledged as collateral against the cash borrowed and reclassified as set forth in paragraph 15(a), and any "rebate" paid to the transferee of securities is interest on the cash the transferor is considered to have borrowed.

94. The transferor of securities being "loaned" accounts for cash received in the same way whether the transfer is accounted for as a sale or a secured borrowing. The cash received shall be recognized as the transferor's asset—as shall investments made with that cash, even if made by agents or in pools with other securities lenders—along with the obligation to return the cash. If securities that may be sold or repledged are received, the transferor of the securities being "loaned" accounts for those securities in the same way as it would account for cash received.

[22]If the "collateral" in a transaction that meets the ~~criteria~~ conditions in paragraph 9 is a financial asset that the holder is permitted by contract or custom to sell or repledge, that financial asset is proceeds of the sale of the "loaned" securities. To the extent that the "collateral" consists of letters of credit or other financial instruments that the holder is not permitted by contract or custom to sell or repledge, a securities lending transaction does not satisfy the sale criteria and is accounted for as a loan of securities by the transferor to the transferee.

Illustration—Securities Lending Transaction Treated as a Secured Borrowing

95. The following example illustrates the accounting for a securities lending transaction treated as a secured borrowing, in which the securities borrower sells the securities upon receipt and later buys similar securities to return to the securities lender:

Facts	
Transferor's carrying amount and fair value of security loaned	$ 1,000
Cash "collateral"	1,020
Transferor's return from investing cash collateral at a 5 percent annual rate	5
Transferor's rebate to the securities borrower at a 4 percent annual rate	4
For simplicity, the fair value of the security is assumed not to change during the 35-day term of the transaction.	

Journal Entries for the Transferor		
At inception:		
Cash	1,020	
Payable under securities loan agreements		1,020
To record the receipt of cash collateral		
Securities pledged to creditors	1,000	
Securities		1,000
To reclassify loaned securities that the secured party has the right to sell or repledge		
Money market instrument	1,020	
Cash		1,020
To record investment of cash collateral		
At conclusion:		
Cash	1,025	
Interest		5
Money market instrument		1,020
To record results of investment		
Securities	1,000	
Securities pledged to creditors		1,000
To record return of security		
Payable under securities loan agreements	1,020	
Interest ("rebate")	4	
Cash		1,024
To record repayment of cash collateral plus interest		

Journal Entries for the Transferee		
At inception:		
Receivable under securities loan agreements	1,020	
Cash		1,020
To record the transfer of cash collateral		
Cash	1,000	
Obligation to return borrowed securities		1,000
To record sale of borrowed securities to a third party and the resulting obligation to return securities that it no longer holds		
At conclusion:		
Obligation to return borrowed securities	1,000	
Cash		1,000
To record the repurchase of securities borrowed		
Cash	1,024	
Receivable under securities loan agreements		1,020
Interest revenue ("rebate")		4
To record the receipt of cash collateral and rebate interest		

Repurchase Agreements and "Wash Sales"

96. Government securities dealers, banks, other financial institutions, and corporate investors commonly use repurchase agreements to obtain or use short-term funds. Under those agreements, the transferor ("repo party") transfers a security to a transferee ("repo counterparty" or "reverse party") in exchange for cash[23] and concurrently agrees to reacquire that security at a future date for an amount equal to the cash exchanged plus a stipulated "interest" factor.

97. Repurchase agreements can be effected in a variety of ways. Some repurchase agreements are similar to securities lending transactions in that the transferee has the right to sell or repledge the securities to a third party during the term of the repurchase agreement. In other repurchase agreements, the transferee does not have the right to sell or repledge the securities during the term of the repurchase agreement. For example, in a tri-party repurchase agreement, the transferor transfers securities to an independent third-party custodian that holds the securities during the term of the repurchase agreement. Also, many repurchase agreements are for short terms, often overnight, or have indefinite terms that allow either party to terminate the arrangement on short notice. However, other repurchase agreements are for longer terms, sometimes until the maturity of the transferred financial asset. Some repurchase agreements call for repurchase of securities that need not be identical to the securities transferred.

98. If the ~~criteria~~ conditions in paragraph 9 are met~~, including the criterion in paragraph 9(c)(1)~~, the transferor shall account for the repurchase agreement as a sale of financial assets and a forward repurchase commitment, and the transferee shall account for the

[23]Instead of cash, other securities or letters of credit sometimes are exchanged. Those transactions are accounted for in the same manner as securities lending transactions (paragraphs 92–94).

agreement as a purchase of financial assets and a forward resale commitment. Other transfers that are accompanied by an agreement to repurchase the transferred financial assets that may ~~shall~~ be accounted for as sales include transfers with agreements to repurchase at maturity and transfers with repurchase agreements in which the [transferor] has not obtained collateral sufficient to fund substantially all of the cost of purchasing replacement financial assets.

99. Furthermore, "wash sales" that previously were not recognized if the same financial asset was purchased soon before or after the sale shall be accounted for as sales under this Statement. Unless there is a concurrent contract to repurchase or redeem the transferred financial assets from the transferee, the transferor does not maintain effective control over the transferred financial assets.

100. As with securities lending transactions, under many agreements to repurchase transferred financial assets before their maturity the transferor maintains effective control over those financial assets. Repurchase agreements that do not meet all the ~~criteria~~ conditions in paragraph 9 shall be treated as secured borrowings. Fixed-coupon and dollar-roll repurchase agreements, and other contracts under which the securities to be repurchased need not be the same as the securities sold, qualify as borrowings if the return of substantially the same (paragraph 48) securities as those concurrently transferred is assured. Therefore, those transactions shall be accounted for as secured borrowings by both parties to the transfer.

101. If a transferor has transferred securities to an independent third-party custodian, or to a transferee, under conditions that preclude the transferee from selling or repledging the assets during the term of the repurchase agreement (as in most tri-party repurchase agreements), the transferor has not surrendered control over those assets.

Loan Syndications

102. Borrowers often borrow amounts greater than any one lender is willing to lend. Therefore, it is common for groups of lenders to jointly fund those loans. That may be accomplished by a syndication under which several lenders share in lending to a single borrower, but each lender loans a specific amount to the borrower and has the right to repayment from the borrower.

103. A loan syndication is not a transfer of financial assets. Each lender in the syndication shall account for the amounts it is owed by the borrower. Repayments by the borrower may be made to a lead lender that then distributes the collections to the other lenders of the syndicate. In those circumstances, the lead lender is simply functioning as a servicer and, therefore, shall not recognize the aggregate loan as a~~n~~ financial asset.

Loan Participations

104. Groups of banks or other entities also may jointly fund large borrowings through loan participations in which a single lender makes a large loan to a borrower and subsequently transfers ~~undivided~~ interests in the loan to other entities.

105. Transfers by the originating lender may take the legal form of either assignments or participations. The transfers are usually on a nonrecourse basis, and the transferor ("originating lender") continues to service the loan. The transferee ("participating entity") may or may not have the right to sell or transfer its participation during the term of the loan, depending upon the terms of the participation agreement.

106. If the loan participation agreement transfers a participating interest in an entire financial asset (as described in paragraph 8B of this Statement) ~~gives the transferee the right to pledge or exchange those participations~~ and the ~~other criteria~~ conditions in paragraph 9 are met, the transfer~~s to the transferee~~ shall be accounted for by the transferor as a sale~~s~~ of a participating interest. ~~financial assets.~~ A transferor's right of first refusal on a bona fide offer from a third party, a requirement to obtain the transferor's permission that shall not be unreasonably withheld, or a prohibition on sale to the transferor's competitor if other potential willing buyers exist is a limitation on the transferee's rights but presumptively does not constrain a transferee from exercising its right to pledge or exchange. However, if the loan participation agreement constrains the transferee~~s~~ from pledging or exchanging ~~their participations~~its participating interest and that constraint provides a more-than-trivial benefit to the transferor~~, the transferor presumptively receives a more than trivial benefit~~, the transferor has not relinquished control ~~over the loan,~~ and shall account for the transfer~~s~~ as a secured borrowing~~s~~.

Banker's Acceptances and Risk Participations in Them

107. Banker's acceptances provide a way for a bank to finance a customer's purchase of goods from a vendor for periods usually not exceeding six months.

Under an agreement between the bank, the customer, and the vendor, the bank agrees to pay the customer's liability to the vendor upon presentation of specified documents that provide evidence of delivery and acceptance of the purchased goods. The principal document is a draft or bill of exchange drawn by the customer that the bank stamps to signify its "acceptance" of the liability to make payment on the draft on its due date.

108. Once the bank accepts a draft, the customer is liable to repay the bank at the time the draft matures. The bank recognizes a receivable from the customer and a liability for the acceptance it has issued to the vendor. The accepted draft becomes a negotiable financial instrument. The vendor typically sells the accepted draft at a discount either to the accepting bank or in the marketplace.

109. A risk participation is a contract between the accepting bank and a participating bank in which the participating bank agrees, in exchange for a fee, to reimburse the accepting bank in the event that the accepting bank's customer fails to honor its liability to the accepting bank in connection with the banker's acceptance. The participating bank becomes a guarantor of the credit of the accepting bank's customer.

110. An accepting bank that obtains a risk participation shall not derecognize the liability for the banker's acceptance, because the accepting bank is still primarily liable to the holder of the banker's acceptance even though it benefits from a guarantee of reimbursement by a participating bank. The accepting bank shall not derecognize the receivable from the customer because it has not transferred the receivable: it controls the benefits inherent in that receivable and it is still entitled to receive payment from the customer. The accepting bank shall, however, record the guarantee purchased, and the participating bank shall record a liability for the guarantee issued.

Illustration—Banker's Acceptance with a Risk Participation

111. An accepting bank assumes a liability to pay a customer's vendor and obtains a risk participation from another bank. The details of the banker's acceptance are provided below:

Facts	
Face value of the draft provided to vendor	$ 1,000
Term of the draft provided to vendor	90 days
Commission with an annual rate of 10 percent	25
Fee paid for risk participation	10

Journal Entries for Accepting Bank		
At issuance of acceptance:		
Receivable from customer	1,000	
Cash	25	
Time draft payable to vendor		1,000
Deferred acceptance commission revenue		25
At purchase of risk participation from a participating bank:		
Guarantee purchased	10	
Cash		10
Upon presentation of the accepted time draft:		
Time draft payable to vendor	1,000	
Deferred acceptance commission revenue	25	
Cash		1,000
Acceptance commission revenue		25
Upon collection from the customer (or the participating bank, if the customer defaults):		
Cash	1,000	
Guarantee expense	10	
Receivable from customer		1,000
Guarantee purchased		10

Journal Entries for Participating Bank		
Upon issuing the risk participation:		
Cash	10	
Guarantee liability		10
Upon payment by the customer to the accepting bank:		
Guarantee liability	10	
Guarantee revenue		10
OR:		
In the event of total default by the customer:		
Guarantee loss	990	
Guarantee liability	10	
Cash (paid to accepting bank)		1,000

Factoring Arrangements

112. Factoring arrangements are a means of discounting accounts receivable on a nonrecourse, notification basis. Accounts receivable in their entireties are sold outright, usually to a transferee (the factor) that assumes the full risk of collection, without recourse to the transferor in the event of a loss. Debtors are directed to send payments to the transferee. Factoring arrangements that meet the ~~criteria~~ conditions in paragraph 9 shall be accounted for as sales of financial assets because the transferor surrenders control over the receivables to the factor.

Transfers of Receivables with Recourse

113. In a transfer of an entire receivable~~s~~, a group of entire receivables, or a portion of an entire receivable with recourse, the transferor provides the transferee with full or limited recourse. A transfer of a portion of

a receivable with recourse does not meet the requirements of a participating interest and shall be accounted for as a secured borrowing. The transferor is obligated under the terms of the recourse provision to make payments to the transferee or to repurchase receivables sold under certain circumstances, typically for defaults up to a specified percentage. The effect of a recourse provision on the application of paragraph 9 may vary by jurisdiction. In some jurisdictions, transfers with full recourse may not place transferred financial assets beyond the reach of the transferor, its consolidated affiliates (that are not entities designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented, and its creditors, but transfers with limited recourse may. A transfer of receivables in their entireties with recourse shall be accounted for as a sale, with the proceeds of the sale reduced by the fair value of the recourse obligation, if the ~~criteria~~ conditions in paragraph 9 are met. Otherwise, a transfer of receivables with recourse shall be accounted for as a secured borrowing.

Extinguishments of Liabilities

114. If a creditor releases a debtor from primary obligation on the condition that a third party assumes the obligation and that the original debtor becomes secondarily liable, that release extinguishes the original debtor's liability. However, in those circumstances, whether or not explicit consideration was paid for that guarantee, the original debtor becomes a guarantor. As a guarantor, it shall recognize a guarantee obligation in the same manner as would a guarantor that had never been primarily liable to that creditor, with due regard for the likelihood that the third party will carry out its obligations. The guarantee obligation shall be initially measured at fair value, and that amount reduces the gain or increases the loss recognized on extinguishment.

~~Appendix C~~

~~ILLUSTRATIVE GUIDANCE~~

~~342. This appendix provides specific examples that illustrate the disclosures that are required by this Statement. The formats in the illustrations are not required by the Statement. The Board encourages entities to use a format that displays the information in the most understandable manner in the specific circumstances. References to paragraphs of this Statement in which the relevant requirements appear are given in parentheses.~~

~~343. The first example illustrates the disclosure of accounting policies for interests that continue to be held by the transferor. In particular, it describes the accounting policies for (a) initial measurement (paragraph 17(h)(1)) and (b) subsequent measurement (paragraph 17(i)(1)), including determination of fair value.~~

> **~~NOTE X—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES~~**
>
> **~~Receivable Sales~~**
>
> ~~When the Company sells receivables in securitizations of automobile loans, credit card loans, and residential mortgage loans, it may hold interest-only strips, one or more subordinated tranches, and in some cases a cash reserve account, all of which are interests that continue to be held by the transferor in the securitized receivables. It may also obtain servicing assets or assume servicing liabilities that are initially measured at fair value. Gain or loss on sale of the receivables depends in part on both (a) the previous carrying amount of the financial assets involved in the transfer, allocated between the assets sold and the interests that continue to be held by the transferor based on their relative fair value at the date of transfer,and (b) the proceeds received. To obtain fair values, quoted market prices are used if available. However, quotes are generally not available for interests that continue to be held by the transferor, so the Company generally estimates fair value based on the present value of future expected cash flows estimated using management's best estimates of the key assumptions—credit losses, prepayment speeds, forward yield curves, and discount rates commensurate with the risks involved.~~

~~344. In addition to the disclosure of assumptions used in determining the values of interests that continue to be held by the transferor at the time of securitization that are presented in paragraph 343, this Statement also requires similar disclosures at the end of the latest period being presented. The following example illustrates disclosures about the characteristics of securitizations and gain or loss from securitizations and other sales by major type of asset (paragraph 17(h)(2)).~~

~~**NOTE Y—SALES OF RECEIVABLES**~~

~~During 20X2 and 20X1, the Company sold automobile loans, residential mortgage loans, and credit card loans in securitization transactions. In all those securitizations, the Company obtained servicing responsibilities and subordinated interests. The Company receives annual servicing fees approximating 0.5 percent (for mortgage loans), 2 percent (for credit card loans), and 1.5 percent (for automobile loans) of the outstanding balance and rights to future cash flows arising after the investors in the securitization trust have received the return for which they contracted. The investors and the securitization trusts have no recourse to the Company's other assets for failure of debtors to pay when due. The interests that continue to be held by the Company are subordinate to investor's interests. Their value is subject to credit, prepayment, and interest rate risks on the transferred financial assets.~~

~~In 20X2, the Company recognized pretax gains of $22.3 million on the securitization of the automobile loans, $30.2 million on the securitization of credit card loans, and $25.6 million on the securitization of residential mortgage loans.~~

~~In 20X1, the Company recognized pretax gains of $16.9, $21.4, and $15.0 million on the securitization of the automobile loans, credit card loans, and residential mortgage loans, respectively.~~

~~345. The following is an illustration of the quantitative information about keyassumptions used in measuring interests that continue to be held by the transferor at the date of sale or securitization for each financial period presented (paragraph 17 (h)(3)).~~

~~Key economic assumptions used in measuring the interests that continue to be held by the transferor at the date of securitization resulting from securitizations completed during the year were as follows (rates* per annum):~~

	20X2				20X1			
			Residential Mortgage Loans				Residential Mortgage Loans	
	Automobile Loans	Credit Card Loans	Fixed Rate	Adjustable ‡	Automobile Loans	Credit Card Loans	Loans	Adjustable‡
Prepayment speed	1.00%	15.00%	10.00%	8.00%	1.00%	12.85%	8.00%	6.00%
Weighted-average life (in years)[33]	1.8	0.4	7.2	6.5	1.8	0.4	8.5	7.2
Expected credit losses	3.10-3.40%	6.10%	1.25%	1.30%	3.50-3.80%	5.30%	1.25%	2.10%
Residual cash flows discounted at	12.0-13.0%	12.00%	10.00%	8.50%	13.00-13.50%	13.00%	11.75%	11.00%
Variable returns to transferees	Forward Eurodollar yield curve plus contractual spread over LIBOR ranging from 30 to 80 basis points		Not applicable		Forward Eurodollar yield curve plus contractual spread over LIBOR ranging from 28 to 70 basis points		Not applicable	

~~**Notes:**~~

~~* Weighted average rates for securitizations entered into during the period for securitizations of loans with similar characteristics.~~

~~‡ Rates for these loans are adjusted based on an index (for most loans, the 1 year Treasury note rate plus 2.75 percent). Contract terms vary, but for most loans, the rate is adjusted every 12 months by no more than 2 percent.~~

~~[33] The weighted average life in periods (for example, months or years) of prepayable assets is calculated by summing the product of (a) the sum of the principal collections expected in each future period times (b) the number of periods until collection, and then dividing that total by (c) the initial principal balance.~~

~~346. The following is an illustration that combines disclosure of the key assumptions used in valuing interests that continue to be held by the transferor at the end of the latest period (paragraph 17(i)(2)) and the hypothetical effect on current fair value of two or more pessimistic variations from the expected levels for each of the key assumptions (paragraph 17(i)(3)).~~

~~At December 31, 20X2, key economic assumptions and the sensitivity of the current fair value of residual cash flows to immediate 10 percent and 20 percent adverse changes in those assumptions are as follows ($ in millions):~~

	Automobile Loans	Credit Card Loans	Residential Mortgage Loans Fixed Rate	Residential Mortgage Loans Adjustable
Carrying amount/fair value of interests that continue to be held by the transferor	$ 15.6	$ 21.25	$ 12.0	$ 13.3
Weighted average life (in years)[34]	1.7	0.4	6.5	6.1
Prepayment speed assumption (annual rate)	**1.3%**	**15.0%**	**11.5%**	**9.3%**
Impact on fair value of 10% adverse change	*$ 0.3*	*$ 1.6*	*$ 3.3*	*$ 2.6*
Impact on fair value of 20% adverse change	*$ 0.7*	*$ 3.0*	*$ 7.8*	*$ 6.0*
Expected credit losses (annual rate)	**3.0%**	**6.1%**	**0.9%**	**1.8%**
Impact on fair value of 10% adverse change	*$ 4.2*	*$ 3.2*	*$ 1.1*	*$ 1.2*
Impact on fair value of 20% adverse change	*$ 8.4*	*$ 6.5*	*$ 2.2*	*$ 3.0*
Residual cash flows discount rate (annual)	**14.0%**	**14.0%**	**12.0%**	**9.0%**
Impact on fair value of 10% adverse change	*$ 1.0*	*$ 0.1*	*$ 0.6*	*$ 0.5*
Impact on fair value of 20% adverse change	*$ 1.8*	*$ 0.1*	*$ 0.9*	*$ 0.9*
Interest rates on variable and adjustable contracts	**Forward Eurodollar yield curve plus contracted spread**			
Impact on fair value of 10% adverse change	*$ 1.5*	*$ 4.0*	*$ 0.4*	*$ 1.5*
Impact on fair value of 20% adverse change	*$ 2.5*	*$ 8.1*	*$ 0.7*	*$ 3.8*

~~These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in fair value based on a 10 percent variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this table, the effect of a variation in a particular assumption on the fair value of the interest that continues to be held by the transferor is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another (for example, increases in market interest rates may result in lower prepayments and increased credit losses), which might magnify or counteract the sensitivities.~~

~~347. The following is an illustration of disclosure of expected static pool credit losses (paragraph 17(i)(2)).~~

Actual and Projected Credit Losses (%) as of:	**Automobile Loans Securitized in 20X0**	**20X1**	**20X2**
December 31, 20X2	5.0	5.9	5.1
December 31, 20X1	5.1	5.0	
December 31, 20X0	4.5		

~~**Note:** Static pool losses are calculated by summing the actual and projected future credit losses and dividing them by the original balance of each pool of assets. The amount shown here for each year is a weighted average for all securitizations during the period.~~

~~[34] Footnote 8, paragraph 17(h)(3), describes how weighted average life can be calculated.~~

~~348. The following is an illustration of the disclosure of cash flows between the securitization SPE and the transferor (paragraph 17(h)(4)).~~

~~The table below summarizes certain cash flows received from and paid to securitization trusts ($ in millions):~~

	Year Ended December 31	
	20X2	20X1
Proceeds from new securitizations	$1,413	$ 971
Proceeds from collections reinvested in previous credit card securitizations	3,150	2,565
Servicing fees received	23	19
Other cash flows received on interests that continue to be held by the transferor*	81	52
Purchases of delinquent or foreclosed assets	(45)	(25)
Servicing advances	(102)	(73)
Repayments of servicing advances	90	63

~~**Note:**~~

~~* This amount represents total cash flows received from interests that continue to be held by the transferor. Other cash flows include, for example, all cash flows from interest-only strips and cash above the minimum required level in cash collateral accounts.~~

~~349. The following illustration presents quantitative information about delinquencies, net credit losses, and components of securitized financial assets and other assets managed together with them ($ in millions):~~

	Total Principal Amount of Loans		Principal Amount of Loans 60 Days or More Past Due*		Average Balances[35]		Net Credit Losses‡	
	At December 31				During the Year			
Type of Loan	20X2	20X1	20X2	20X1	20X2	20X1	20X2	20X1
Automobile loans	$ 830	$ 488	$ 42.3	$ 26.8	$ 720	$ 370	$ 21.6	$ 12.6
Residual mortgage loans (fixed rate)	482	302	5.8	3.6	470	270	5.6	3.2
Residual mortgage loans (adjustable)	544	341	7.1	6.8	520	300	6.2	6.0
Credit card loans	300	250	15	12.5	350	300	16	15
Total loans managed or securitized†	2,156	1,381	$ 70.2	$ 49.7	2,060	1,240	$ 49.4	$ 36.8
Less:								
Loans securitized§	1,485	905			1,368	752		
Loans held for sale or securitization	19	11			17	9		
Loans held in portfolio[36]	$ 652	$ 465			$ 675	$ 479		

~~**Notes:**~~

~~* Loans 60 days or more past due are based on end of period total loans.~~

~~‡ Net credit losses are charge offs and are based on total loans outstanding.~~

~~† Owned and securitized loans are customer loans, credit card loans, mortgage loans, auto loans, and other loans, as applicable, in which the transferor retains a subordinate interest or retains any risk of loss (for example, 10 percent recourse).~~

~~§ Represents the principal amount of the loan. Interest only strips (or other interests that continue to be held by a transferor) and servicing assets and servicing liabilities held for securitized assets are excluded from this table because they are recognized separately.~~

~~[35] This disclosure is optional.~~

~~[36] Loans held in portfolio are reported separately from loans held for securitization because they are measured differently.~~

~~349A. The following is an illustration of disclosures related to the activity in the balance of servicing assets and servicing liabilities by class (paragraphs 17(f)(1) and 17(g)(1)):~~

~~Tabular Disclosures of Changes in Servicing Assets and Servicing Liabilities Subsequently Measured Using the Fair Value Measurement Method~~

	~~Class 1~~		~~Class 2~~		
~~Balance Sheet Disclosures~~	**~~Servicing Asset~~**	**~~Servicing Liability~~**	**~~Servicing Asset~~**	**~~Servicing Liability~~**	**~~Reference~~**
~~Fair value as of the beginning of the period~~	~~XX~~	~~XX~~	~~XX~~	~~XX~~	~~17(f)(1)(a)~~
~~Additions:~~					~~17(f)(1)(b)~~
~~Purchases of servicing assets~~	~~XX~~	~~N/A~~	~~XX~~	~~N/A~~	
~~Assumption of servicing obligations~~	~~XX~~	~~XX~~	~~XX~~	~~XX~~	
~~Servicing obligations that result from transfers of financial assets~~	~~XX~~	~~XX~~	~~XX~~	~~XX~~	
~~Subtractions:~~					
~~Disposals~~	~~(XX)~~	~~(XX)~~	~~(XX)~~	~~(XX)~~	~~17(f)(1)(c)~~
~~Changes in fair value:~~					~~17(f)(1)(d)~~
~~Due to change in valuation inputs or assumptions used in valuation model~~	~~XX/(XX)~~	~~XX/(XX)~~	~~XX/(XX)~~	~~XX/(XX)~~	
~~Other changes in fair value~~	~~XX/(XX)~~	~~XX/(XX)~~	~~XX/(XX)~~	~~XX/(XX)~~	
~~Other changes that affect the balance~~	~~XX/(XX)~~	~~XX/(XX)~~	~~XX/(XX)~~	~~XX/(XX)~~	~~17(f)(1)(e)~~
~~Fair value as of the end of the period~~	~~XX~~	~~XX~~	~~XX~~	~~XX~~	~~17(f)(1)(a)~~

~~Tabular Disclosures of Changes in Servicing Assets and Servicing Liabilities Subsequently Measured Using the Amortization Method~~

	~~Class 3~~		~~Class 4~~		
~~Balance Sheet Disclosures~~	**~~Servicing Asset~~**	**~~Servicing Liability~~**	**~~Servicing Asset~~**	**~~Servicing Liability~~**	**~~Reference~~**
~~Carrying amount as of the beginning of the period~~	~~XX~~	~~XX~~	~~XX~~	~~XX~~	~~17(g)(1)(a)~~
~~Additions:~~					~~17(g)(1)(b)~~
~~Purchases of servicing assets~~	~~XX~~	~~N/A~~	~~XX~~	~~N/A~~	
~~Assumption of servicing obligations~~	~~XX~~	~~XX~~	~~XX~~	~~XX~~	
~~Servicing obligations that result from transfers of financial assets~~	~~XX~~	~~XX~~	~~XX~~	~~XX~~	
~~Subtractions:~~					
~~Disposals~~	~~(XX)~~	~~(XX)~~	~~(XX)~~	~~(XX)~~	~~17(g)(1)(c)~~
~~Amortization~~	~~(XX)~~	~~(XX)~~	~~(XX)~~	~~(XX)~~	~~17(g)(1)(d)~~
~~Application of valuation allowance to adjust carrying values of servicing assets~~	~~XX/(XX)~~	~~N/A~~	~~XX/(XX)~~	~~N/A~~	~~17(g)(1)(e)~~
~~Other-than-temporary impairments~~	~~(XX)~~	~~(XX)~~	~~(XX)~~	~~(XX)~~	~~17(g)(1)(f)~~
~~Other changes that affect the balance~~	~~XX/(XX)~~	~~XX/(XX)~~	~~XX/(XX)~~	~~XX/(XX)~~	~~17(g)(1)(g)~~
~~Carrying amount before valuation allowance~~	~~XX~~	~~XX~~	~~XX~~	~~XX~~	
~~Valuation allowance for servicing assets:~~					~~17(g)(5)~~
~~Beginning balance~~	~~XX~~	~~N/A~~	~~XX~~	~~N/A~~	
~~Provisions/recoveries~~	~~XX/(XX)~~	~~N/A~~	~~XX/(XX)~~	~~N/A~~	
~~Other-than-temporary impairments~~	~~(XX)~~	~~N/A~~	~~(XX)~~	~~N/A~~	~~17(g)(1)(f)~~
~~Sales and disposals~~	~~(XX)~~	~~N/A~~	~~(XX)~~	~~N/A~~	
~~Ending balance~~	~~XX/(XX)~~	~~N/A~~	~~XX/(XX)~~	~~N/A~~	
~~Carrying amount as of the end of the period~~	~~XX~~	~~XX~~	~~XX~~	~~XX~~	~~17(g)(1)(a)~~
~~Fair Value Disclosures~~					
~~Fair value as of the beginning of the period~~	~~XX~~	~~XX~~	~~XX~~	~~XX~~	~~17(g)(2)~~
~~Fair value as of the end of the period~~	~~XX~~	~~XX~~	~~XX~~	~~XX~~	~~17(g)(2)~~

Appendix E

GLOSSARY

364. This appendix defines terms used in this Statement.

Adequate compensation
The amount of benefits of servicing that would fairly compensate a substitute servicer should one be required, which includes the profit that would be demanded in the marketplace.

Agent
A party that acts for and on behalf of another party. For example, a third-party intermediary is an agent of the transferor if it acts on behalf of the transferor.

Attached call
A call option held by the transferor of a financial asset that becomes part of and is traded with the underlying instrument. Rather than being an obligation of the transferee, an attached call is traded with and diminishes the value of the underlying instrument transferred subject to that call.

Beneficial interests
Rights to receive all or portions of specified cash inflows ~~to~~ received by a trust or other entity, including, but not limited to, senior and subordinated shares of interest, principal, or other cash inflows to be "passed-through" or "paid-through," premiums due to guarantors, commercial paper obligations, and residual interests, whether in the form of debt or equity.

Benefits of servicing
Revenues from contractually specified servicing fees, late charges, and other ancillary sources, including "float."

Cleanup call
An option held by the servicer or its affiliate, which may be the transferor, to purchase the remaining transferred financial assets, or the remaining beneficial interests not held by the transferor, its affiliates, or its agents in an ~~qualifying SPE~~ entity (or in a series of beneficial interests in transferred financial assets within an ~~qualifying SPE~~ entity), if the amount of outstanding financial assets or beneficial interests falls to a level at which the cost of servicing those assets or beneficial interests becomes burdensome in relation to the benefits of servicing.

Collateral
Personal or real property in which a security interest has been given.

Consolidated affiliate ~~of the transferor~~
An entity whose assets and liabilities are included with those of the transferor in the consolidated, combined, or other financial statements being presented.

Continuing involvement
Any involvement with the transferred financial assets that permits the transferor to receive cash flows or other benefits that arise from the transferred financial assets or that obligates the transferor to provide additional cash flows or other assets to any party related to the transfer. All available evidence shall be considered, including, but not limited to, explicit written arrangements, communications between the transferor and the transferee or its beneficial interest holders, and unwritten arrangements customary in similar transfers. Examples of continuing involvement with the transferred financial assets include, but are not limited to, servicing arrangements, recourse or guarantee arrangements, agreements to purchase or redeem transferred financial assets, options written or held, derivative financial instruments that are entered into contemporaneously with, or in contemplation of, the transfer, arrangements to provide financial support, pledges of collateral, and the transferor's beneficial interests in the transferred financial assets.

Contractually specified servicing fees
All amounts that, per contract, are due to the servicer in exchange for servicing the financial asset and would no longer be received by a servicer if the beneficial owners of the serviced assets (or their trustees or agents) were to exercise their actual or potential authority under the contract to shift the servicing to another servicer. Depending on the servicing contract, those fees may include some or all of the difference between the interest

rate collectible on the financial asset being serviced and the rate to be paid to the beneficial owners of those financial assets.

Derecognize

Remove previously recognized assets or liabilities from the statement of financial position.

Derivative financial instrument

A derivative instrument (as defined in Statement 133) that is a financial instrument (refer to Statement 107, paragraph 3).

Embedded call

A call option held by the issuer of a financial instrument that is part of and trades with the underlying instrument. For example, a bond may allow the issuer to call it by posting a public notice well before its stated maturity that asks the current holder to submit it for early redemption and provides that interest ceases to accrue on the bond after the early redemption date. Rather than being an obligation of the initial purchaser of the bond, an embedded call trades with and diminishes the value of the underlying bond.

Financial asset

Cash, evidence of an ownership interest in an entity, or a contract that conveys to [one] entity a right (a) to receive cash or another financial instrument from a [second] entity or (b) to exchange other financial instruments on potentially favorable terms with the [second] entity.

Financial liability

A contract that imposes on one entity [an] obligation (a) to deliver cash or another financial instrument to a second entity or (b) to exchange other financial instruments on potentially unfavorable terms with the second entity.

Freestanding call

A call that is neither embedded in nor attached to an asset subject to that call.

~~**Guaranteed mortgage securitization**~~

~~A securitization of mortgage loans that is within the scope of FASB Statement No. 65, *Accounting for Certain Mortgage Banking Activities,* as amended, and includes a substantive guarantee by a third party.~~

Interest-only strip

A contractual right to receive some or all of the interest due on a bond, mortgage loan, collateralized mortgage obligation, or other interest-bearing financial asset.

Participating interest

A participating interest has the following characteristics:

a. From the date of the transfer, it represents a proportionate (pro rata) ownership interest in an entire financial asset. The percentage of ownership interests held by the transferor in the entire financial asset may vary over time, while the entire financial asset remains outstanding as long as the resulting portions held by the transferor (including any participating interest retained by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents) and the transferee(s) meet the other characteristics of a participating interest. For example, if the transferor's interest in an entire financial asset changes because it subsequently sells another interest in the entire financial asset, the interest held initially and subsequently by the transferor must meet the definition of a participating interest.
b. From the date of the transfer, all cash flows received from the entire financial asset are divided proportionately among the participating interest holders in an amount equal to their share of ownership. Cash flows allocated as compensation for services performed, if any, shall not be included in that determination provided those cash flows are not subordinate to the proportionate cash flows of the participating interest and are not significantly above an amount that would fairly compensate a substitute service provider, should one be required, which includes the profit that would be demanded in the marketplace. In addition, any cash flows received by the transferor as proceeds of the transfer of the participating interest shall be excluded from the determination of proportionate cash flows provided that the transfer does not result in the transferor receiving an ownership interest in the financial asset that permits it to receive disproportionate cash flows.

c. The rights of each participating interest holder (including the transferor in its role as a participating interest holder) have the same priority, and no participating interest holder's interest is subordinated to the interest of another participating interest holder. That priority does not change in the event of bankruptcy or other receivership of the transferor, the original debtor, or any other participating interest holder. Participating interest holders have no recourse to the transferor (or its consolidated affiliates included in the financial statements being presented or its agents) or to each other, other than standard representations and warranties, ongoing contractual obligations to service the entire financial asset and administer the transfer contract, and contractual obligations to share in any set-off benefits received by any participating interest holder. That is, no participating interest holder is entitled to receive cash before any other participating interest holder under its contractual rights as a participating interest holder. For example, if a participating interest holder also is the servicer of the entire financial asset and receives cash in its role as servicer, that arrangement would not violate this requirement.
d. No party has the right to pledge or exchange the entire financial asset unless all participating interest holders agree to pledge or exchange the entire financial asset.

Proceeds
Cash, beneficial interests, servicing assets, derivatives, or other assets that are obtained in a transfer of financial assets, less any liabilities incurred.

Recourse
The right of a transferee of receivables to receive payment from the transferor of those receivables for (a) failure of debtors to pay when due, (b) the effects of prepayments, or (c) adjustments resulting from defects in the eligibility of the transferred receivables.

Securitization
The process by which financial assets are transformed into securities.

Security interest
A form of interest in property that provides that upon default of the obligation for which the security interest is given, the property may be sold in order to satisfy that obligation.

Seller
A transferor that relinquishes control over financial assets by transferring them to a transferee in exchange for consideration.

Servicing asset
A contract to service financial assets under which the estimated future revenues from contractually specified servicing fees, late charges, and other ancillary revenues are expected to more than adequately compensate the servicer for performing the servicing. A servicing contract is either (a) undertaken in conjunction with selling or securitizing the financial assets being serviced or (b) purchased or assumed separately.

Servicing liability
A contract to service financial assets under which the estimated future revenues from contractually specified servicing fees, late charges, and other ancillary revenues are not expected to adequately compensate the servicer for performing the servicing.

Standard representations and warranties
Representations and warranties that assert the financial asset being transferred is what it is purported to be at the transfer date. Examples include representations and warranties about (a) the characteristics, nature, and quality of the underlying financial asset, including characteristics of the underlying borrower and the type and nature of the collateral securing the underlying financial asset, (b) the quality, accuracy, and delivery of documentation relating to the transfer and the underlying financial asset, and (c) the accuracy of the transferor's representations in relation to the underlying financial asset.

Transfer
The conveyance of a noncash financial asset by and to someone other than the issuer of that financial asset. Thus, a transfer includes selling a receivable, putting it into a securitization trust, or

posting it as collateral but excludes the origination of that receivable, the settlement of that receivable, or the restructuring of that receivable into a security in a troubled debt restructuring.

Transferee

An entity that receives a financial asset, an interest in ~~a portion of~~ a financial asset, or a group of financial assets from a transferor.

Transferor

An entity that transfers a financial asset, an interest in ~~a portion of~~ a financial asset, or a group of financial assets that it controls to another entity.

~~**Undivided interest**~~

~~Partial legal or beneficial ownership of an asset as a tenant in common with others. The proportion owned may be pro rata, for example, the right to receive 50 percent of all cash flows from a security, or non–pro rata, for example, the right to receive the interest from a security while another has the right to the principal.~~

Unilateral ability

A capacity for action not dependent on the actions (or failure to act) of any other party.