NO. 1610-100 | SEPTEMBER 15, 2008

Financial Accounting Series

EXPOSURE DRAFT (Revised)

Proposed Statement of Financial Accounting Standards

Accounting for Transfers of Financial Assets

an amendment of FASB Statement No. 140

Revision of Exposure Draft
Issued August 11, 2005

This Exposure Draft of a proposed Statement of Financial Accounting Standards is issued by the Board for public comment. Written comments should be addressed to:

Technical Director
File Reference No. 1610-100

Comment Deadline: November 14, 2008

Financial Accounting Standards Board
of the Financial Accounting Foundation

Responses from interested parties wishing to comment on the Exposure Draft must be **received** in writing by November 14, 2008. Interested parties should submit their comments by email to director@fasb.org, File Reference No.1610-100. Those without email may send their comments to the "Technical Director—File Reference No. 1610-100" at the address at the bottom of this page. Responses should **not** be sent by fax.

All comments received by the FASB are considered public information. Those comments will be posted to the FASB's website and will be included in the project's public record.

An electronic copy of this Exposure Draft is available on the FASB's website until the FASB issues a final document. Any individual or organization may obtain one copy of this Exposure Draft without charge until November 14, 2008, on written request only. **Please ask for our Product Code No. E198**. For information on applicable prices for additional copies and copies requested after November 14, 2008, contact:

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Notice for Recipients of This Exposure Draft

This proposed Statement, which is a revision of the August 2005 FASB Exposure Draft, *Accounting for Transfers of Financial Assets*, would remove (1) the concept of a qualifying special-purpose entity (SPE) from FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* and (2) the exceptions from applying FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities,* to qualifying SPEs. This proposed Statement also would amend Statement 140 to revise and clarify the derecognition requirements for transfers of financial assets and the initial measurement of beneficial interests that are received as proceeds by a transferor in connection with transfers of financial assets. This proposed Statement also would enhance the disclosure requirements to provide users of financial statements with greater transparency about transfers of financial assets and a transferor's continuing involvement with such transferred financial assets.

This proposed Statement is being exposed concurrently with the proposed FASB Statement, *Amendments to FASB Interpretation No. 46(R),* which would amend the consolidation and related disclosure requirements for enterprises that hold an interest in a variable interest entity. Most securitization entities that previously met the requirements of a qualifying SPE under Statement 140 that are variable interest entities would now be required to be evaluated under the revised guidance in the proposed Statement on amendments to Interpretation 46(R), including entities that transfer financial assets, hold a variable interest in such an entity, or both.

Effective Date and Transition

This proposed Statement would be effective as of the beginning of a reporting entity's first fiscal year that begins after November 15, 2009. Earlier application would be prohibited.

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

Request for Comments

The Board invites individuals and organizations to send written comments on all matters in this proposed Statement, particularly on the questions listed below. Respondents need not comment on each issue and are encouraged to comment on additional matters they believe should be brought to the Board's attention. Comments are requested from those who agree with the provisions of this proposed Statement as well as from those who do not. Comments are most helpful if they identify the issues to which they relate and clearly explain the reasons for the positions taken. Those who disagree with provisions of this proposed Statement are asked to describe their suggested alternatives, supported by specific reasoning. Respondents must submit comments in writing by November 14, 2008.

The Board requests that constituents provide comments on the following questions:

1. Will the proposed Statement meet the project's objective to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about (a) a transfer of financial assets, (b) the effects of a transfer on its financial position, financial performance, and cash flows, and (c) a transferor's continuing involvement in transferred financial assets?
2. Do you agree with the Board's decisions to eliminate the qualifying SPE concept and to require that all securitization entities be evaluated for consolidation under applicable U.S. generally accepted accounting principles? If not, why not?
3. Certain financial statement users suggested that the Board adopt a no-continuing-involvement model (that is, if there is *any* continuing involvement, sale accounting would not be permitted). The Board decided to continue to permit derecognition of financial assets with continuing involvement as long as the conditions in paragraph 9 of Statement 140, as amended by this proposed Statement, are met, with the addition of enhanced disclosure requirements about a transferor's continuing involvement (see paragraph A28 of this proposed Statement). Do you agree with this decision? If not, why do you disagree and what approach would you recommend to meet the needs of financial statement users for additional information on transferred financial assets?
4. What costs do you expect to incur if the Board were to issue this proposed Statement in its current form as a final Statement? How could the Board further reduce the costs of applying these requirements without significantly reducing the benefits?
5. The Board decided to establish specific conditions for reporting a transfer of a portion of a financial asset as a sale. A transfer of a portion of a financial asset as a sale is eligible for derecognition only for a pro rata portion that meets the definition of a participating interest. Do you agree with this decision? If not, why do you disagree? If you agree with the Board's decision to limit the portions of a financial asset that are eligible for derecognition, do you agree with the definition of a participating interest? If not, what alternative definition do you recommend and why?
6. Paragraph 9(c) of Statement 140 and the related implementation guidance, as amended by this proposed Statement, require that the transferor (a) not maintain effective control over transferred financial assets to account for a transfer as a sale and (b) provide examples of effective control. The Board decided to incorporate many of the concepts from paragraph 9(b) of Statement 140 into paragraph 9(c), which results in the creation of the additional examples that are included in paragraphs 9(c)(3) and 9(c)(4). Do you believe that paragraph 9(c) of Statement 140 and the related implementation guidance, as amended by this proposed Statement, clearly explain how to determine if the transferor maintains effective control? If not, what additional guidance or

examples are necessary? Do you believe that paragraph 9(c), as amended by this proposed Statement, is operational in its entirety in its current form? If not, what changes are necessary? Do you believe these additional examples of effective control in paragraphs 9(c)(3) and 9(c)(4) are operational in their current form? If not, what changes are necessary?

7. Certain financial statement users strongly recommended that the Board provide disclosure principles and require certain specific disclosures for both transferred financial assets treated as sales and those that are treated as secured borrowings. Do you agree that additional disclosures about transferred financial assets are necessary and operational? If not, what changes would you make to the requirements? Do you believe that the revisions to the disclosure requirements are sufficient? If not, what additional disclosures do you believe are necessary?
8. Appendix C includes significant amendments, primarily as a result of this proposed Statement, to related literature including (a) the FASB Special Report, *A Guide to Implementation of Statement 140 on Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, (b) certain Emerging Issues Task Force (EITF) Issues and Topics, and (c) certain AICPA Audit and Accounting Guides. Do you agree that the related literature, as amended, is consistent with the proposed amendments to Statement 140? If not, why do you disagree and what changes would you make?
9. Due to differences in financial statement user needs and cost-benefit considerations, should any differences exist for recognition, measurement, disclosure, transition, or effective date for private companies? If yes, please articulate what differences should exist and the reasons for those differences.

Public Roundtable Meeting

The Board plans to hold a public roundtable meeting on this Exposure Draft on November 6, 2008. The purpose of roundtable meetings is to listen to the views of, and obtain information from, interested constituents about the Exposure Draft. The Board plans to seek participants for the meetings that represent a wide variety of constituents, including financial statement users, preparers, auditors, and others to ensure that it receives broad input. Any individual or organization desiring to participate must notify the FASB by sending an email to director@fasb.org by October 27, 2008, and submitting their comments on the Exposure Draft in writing by October 30, 2008. Roundtable meetings can accommodate a limited number of participants. Depending on the number of responses received, the Board may not be able to accommodate all requests to participate.

Summary

WHY IS THE FASB ISSUING THIS PROPOSED STATEMENT AND WHEN WILL IT BE EFFECTIVE?

The Board's objective in issuing this proposed 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 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 proposed Statement would be applied to transfers occurring on or after the beginning of a reporting entity's first fiscal year that begins after November 15, 2009. Earlier application would be prohibited.

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

What Is the Scope of This Proposed Statement?

This proposed Statement has the same scope as Statement 140. Accordingly, this proposed Statement would apply to all entities.

How Will This Proposed Statement Change Current Practice?

This proposed Statement would remove the concept of a qualifying SPE from Statement 140 and would remove the exception from applying Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities,* to qualifying SPEs.

This proposed Statement would clarify that the objective of paragraph 9 of Statement 140, as amended by this proposed Statement, and related guidance is to determine whether a transferor and all of the entities included in the financial statements being presented have surrendered control over transferred financial assets. This determination 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.

This proposed Statement would define 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, sale accounting could be achieved only by transferring an entire financial asset or a group of financial assets that meet the derecognition criteria in paragraph 9 of Statement 140, as amended by this proposed Statement.

The special provisions in Statement 140 and FASB Statement No. 65, *Accounting for Certain Mortgage Banking Activities,* for guaranteed mortgage securitizations would be removed 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 proposed Statement. If such a transfer does not meet the requirements for sale accounting, the securitized mortgage loans would continue to be classified as loans.

The use of fair value measurements would be increased because this proposed Statement would require a transferor's beneficial interests to be considered an asset obtained as proceeds that is initially measured at fair value when the transfer is accounted for as a sale. This proposed Statement also would eliminate the fair value practicability exceptions in Statement 140.

Enhanced disclosures would be required to provide users of financial statements with greater transparency about transfers of financial assets and a transferor's continuing involvement with such transferred financial assets.

How Will This Proposed Statement Improve Financial Reporting?

This proposed Statement would improve financial reporting by eliminating (1) the exceptions for qualifying SPEs from the consolidation guidance and (2) 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 would be improved through clarifications of the requirements for isolation and limitations on portions of financial assets that are eligible for sale accounting.

This proposed Statement would enhance the information provided to users of financial statements about transfers of financial assets and a transferor's continuing involvement with transferred financial assets. This proposed Statement would require that many types of transferred financial assets that would have been derecognized previously would no longer be eligible for derecognition, and it would require enhanced disclosures about the risks that a transferor continues to be exposed to from its continuing involvement in transferred financial assets.

This proposed Statement also would clarify and improve 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 Proposed Statement on Convergence with International Financial Reporting Standards?

The International Accounting Standards Board (IASB) has a project on its agenda to develop a new standard on derecognition that is more consistent with the IASB conceptual framework of financial reporting. In July 2008, the IASB moved this project from its research agenda to its active agenda. Ultimately, the two Boards will seek to issue a converged derecognition standard.

This proposed Statement is designed 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 IASB.

In the short term, this project improves convergence by eliminating the concept of a qualifying SPE, 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*.

Proposed Statement of Financial Accounting Standards

Accounting for Transfers of Financial Assets

an amendment of FASB Statement No. 140

September 15, 2008

CONTENTS

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Accounting for Transfers of Financial Assets

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September 15, 2008

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. To accomplish that, 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 (SPE) from Statement 140 and removes the exception from applying FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities,* to qualifying SPEs.
b. 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 financial assets in a transfer that meets the derecognition criteria in paragraph 9 of Statement 140, as amended by this Statement.
c. 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.
d. 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 criteria in paragraph 9 of Statement 140, as amended by this Statement.

e. It clarifies the isolation analysis to ensure that the financial asset has been put beyond the reach of the transferor and its consolidated affiliates, except for certain bankruptcy-remote entities, included in the financial statements being presented.
f. It requires the transferor to evaluate whether it, its consolidated affiliates included in the financial statements being presented, or its agents effectively control the transferred financial asset. For example, if the transferee is constrained from pledging or exchanging the transferred financial asset and such constraint is not designed primarily to provide a benefit to the transferee, the transferor maintains effective control over the transferred financial asset.
g. It requires a transferor's proceeds to be initially measured at fair value when the transfer is accounted for as a sale.
h. 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 requirements for sale accounting, the securitized mortgage loans will continue to be classified as loans.
i. It requires enhanced disclosures to provide financial statement users with greater transparency regarding transfers of financial assets and a transferor's continuing involvement with such transferred financial assets.

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 <u>underlined</u> 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 <u>financial</u> 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 are **recourse**, servicing,

agreements to reacquire, options written or held, and pledges of **collateral**. 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~~ interest that continues to be held by a transferor becomes an asset separate from the ~~portion~~ interest sold and from the assets obtained in exchange.

d. Paragraph 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.

e. Paragraph 7A is added as follows:

The Board issued Statement 125 in June 1996. The Board received a number of requests subsequent to the issuance of Statement 125 to reconsider or clarify the conditions for sale accounting and to expand the disclosure requirements in Statement 125. In response to those requests, the Board decided to amend Statement 125 and to replace it with Statement 140, even though most of the provisions of Statement 125 were carried forward to Statement 140 without reconsideration. The Board continued to receive requests from preparers and auditors to address various application issues. The Board decided to undertake a project to amend Statement 140 to address those concerns. During that project, in response to significant events in the credit markets, financial statement users requested limitations on sale accounting and additional disclosures. The Board concluded that a number of changes to the derecognition model were necessary to identify situations in which a transferor continues to maintain control of the transferred financial assets to such an extent that derecognition of the financial assets was not appropriate. The Board decided to amend Statement 140 with Statement 16X in 2008 to strengthen the guidance on control and to require additional disclosures.

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

<u>8A. The objective of paragraph 9 and related guidance is to determine whether a transferor and all of the entities included in the financial statements being presented have surrendered control over transferred financial assets. This determination must consider all arrangements or</u>

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 individual financial asset in its entirety, transfers of groups of financial assets in their entirety, and transfers of a **participating interest** in an individual financial asset (which are referred to collectively in this Statement as *transferred financial assets*). A participating interest has the following characteristics:

a. It represents a proportionate ownership interest in an entire individual financial asset other than an equity instrument, a **derivative financial instrument,** or a hybrid financial instrument with an embedded derivative that is not clearly and closely related as described in Statement 133.
b. All cash flows received from the asset are divided among the participating interests (including any interest retained by the transferor, its **consolidated affiliates** included in the financial statements being presented, or its **agents**) in proportion to the share of ownership represented by each. Cash flows allocated to a servicer as compensation for servicing activities, if any, shall not be included in that determination. The transferor's ownership shares must remain pro rata over the life of the original financial asset. Participating interests may be further apportioned by the transferor as long as the resulting portions meet the definition of a participating interest.
c. The rights of each participating interest holder (including the transferor if it retains a participating interest) have the same priority, and that priority does not change in the event of bankruptcy or other receivership of the transferor, the original debtor, or any participating interest holder. Participating interest holders have no recourse, other than standard representations and warranties, to the transferor (or its consolidated affiliates included in the financial statements being presented or agents) or to each other, and no participating interest holder is subordinated to another. That is, no participating interest holder is entitled to receive cash before any other participating interest holder in its role as a participating interest holder.
d. No party has the right to pledge or exchange the entire financial asset.

If a transfer of a portion of an individual 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 an individual 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.

h. Paragraph 9:

A transfer of an individual financial asset in its entirety, a group of financial assets in their entirety, or a participating interest in an individual 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 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 included in the financial statements being presented. For multiple step transfers, a special-purpose entity (SPE)[2a] 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[2b] (paragraphs 27, 28, and 83).

~~b. Each transferee (or, if the transferee is a qualifying SPE (paragraph 35), each 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 holder) from taking advantage of its right to pledge or exchange and provides more than a trivial benefit to the transferor (paragraphs 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. Judgment is required to assess whether a particular agreement provides the transferor with effective control of the transferred financial asset. For example, effective control over the transferred financial assets by the transferor exists 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) the ability to unilaterally cause the holder to return specific financial assets, other than through a **cleanup call** (paragraphs 50–54), (3) a restriction on the transferee's right to pledge or exchange the transferred financial asset it receives unless such constraint is designed primarily to provide the transferee with a benefit (paragraphs 54A–54D), or (4) 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 the transferred financial assets (paragraph 54E).

[2a]For purposes of this Statement, the term *SPE* includes, but is not limited to, any entity whose activities are primarily related to securitization or other forms of asset-backed financings.
[2b]Notwithstanding the isolation analysis, each SPE involved in the transfer is subject to the applicable guidance on whether it must be consolidated. For additional guidance on the isolation analysis, see paragraph 83.

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

a. Allocate the previous carrying amount between the participating interests sold and the participating interest that continues to be held by the transferor based on their relative fair values at the date of the transfer (paragraphs 58–60)
b. Derecognize the participating interest or interests sold
c. Recognize and initially measure at fair value assets obtained or liabilities incurred, including servicing assets or servicing liabilities, from the sale of the participating interest(s)
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 and the amount derecognized.

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

[2c]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, 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 Financial Assets

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

a. Derecognize ~~all~~the transferred financial assets in their entirety~~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 (paragraphs 56–59 and 61–66), and any other assets obtained (including the transferor's **beneficial interest** or any other interests in the transferred financial assets) and liabilities incurred[3a] in the sale~~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 2c.~~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 individual financial asset in its entirety or a group of financial assets in their entirety 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 individual financial asset~~s~~ in its entirety, a group of financial assets in their entirety, or a participating interest in an individual financial asset 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~~,~~ or if a transfer of a portion of an individual financial asset does not meet the definition of a participating interest, 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.

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 any of the following situations:

a. A transfer of a servicer's individual financial asset in its entirety, a group of the servicer's financial assets in their entirety, or a participating interest in a servicer's individual financial asset ~~the servicer's financial assets~~ that meets the requirements for sale accounting

~~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 in which the transferor retains all of 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.~~

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 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, 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. Paragraphs 16A–16C are added as follows under the heading "Disclosures":

> 16A. The principal objectives of the disclosures required by paragraph 17 are to provide users of the financial statements with an understanding of:
>
> a. A transferor's continuing involvement in financial assets that it has transferred to an SPE
> b. The nature of any restrictions on assets reported by an entity in its statement of financial position, including the carrying amounts of such assets
> c. How servicing assets and servicing liabilities are reported under this Statement
> d. How a transfer of financial assets affects an entity's financial position, financial performance, and cash flows.
>
> A reporting entity shall consider these overall objectives in providing the disclosures required by this Statement.
>
> 16B. Disclosures required by this Statement may be reported in the aggregate for similar transfers if separate reporting of each transfer would not add useful incremental information to financial statement users. However, a transferor must distinguish transfers that are accounted for as sales from transfers that are accounted for as secured borrowings. A transferor shall disclose how similar transfers are aggregated. In determining whether to aggregate the disclosures for multiple transfers, the reporting entity shall consider quantitative and qualitative information about the characteristics of the financial assets transferred. 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.

16C. To apply the disclosures in paragraph 17, all involvements by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents shall be considered involvement by the transferor.

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

In addition to the disclosures required by other standards, a~~A~~n entity shall disclose the following:

a. If assets are restricted solely to satisfy a specific obligation, the carrying amount of those assets and associated liabilities, including a description of the nature of restrictions placed on the assets.

~~a~~b. 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 amount and classification of those assets as of the date of the latest statement of financial position presented

(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~~c. 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. For all servicing assets and servicing liabilities:
   (1) Management's basis for determining its classes of servicing assets and servicing liabilities (see 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.

f. 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 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, 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(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. 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, assumption of servicing obligations, and 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, 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(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) 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) 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. If the entity has ~~securitized~~transferred financial assets to an SPE 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) 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~~

(1~~2~~) The characteristics of the transfer ~~securitizations~~ (including a description of the transferor's continuing involvement with the transferred financial assets, if any~~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 financial assets~~ in securitizations~~, including quantitative information about how the gain or loss was determined

(2~~3~~) The methodology, key inputs, and assumptions[7] used in measuring the fair value of assets obtained (including the transferor's beneficial interests and any other interests in the transferred financial assets) and liabilities incurred in the sale~~interests that continue to be held by the transferor and servicing assets or servicing liabilities~~, if any, at the time of transfer~~securitization~~ (including, at a minimum, 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~~)

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

i. If the ~~entity has interests that continue to be held by the~~ transferor has continuing involvement in financial assets that it has ~~securitized~~transferred to an SPE (including those transfers that are accounted for as sales and those that are accounted for as secured borrowings) ~~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)~~:

(1) Qualitative and quantitative information about the transfer, giving consideration to both explicit and implicit arrangements, that provides users with sufficient information to assess 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:

- (a) The transferor's continuing involvement with the transferred financial assets
- (b) The carrying amount and classification of assets and associated liabilities recognized in the transferor's statement of financial position at the reporting date, including qualitative information about the relationship(s) between those assets and associated liabilities
- (c) The terms of any arrangements that could require the transferor to provide financial support (for example, liquidity commitments 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
- (d) 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:
  - (i) The type and amount of noncontractual support
  - (ii) The primary reasons for providing the noncontractual support
- (e) Liquidity, guarantees, and other commitments provided by third parties related to the transferred financial assets

(2~~1~~) Its accounting policies for subsequently measuring ~~those interests~~any assets or liabilities that relate to the continuing involvement in 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~~

(3~~2~~) The methodology, key inputs, and assumptions 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, if applicable, quantitative information about discount rates, expected prepayments including the expected weighted-average life of prepayable financial assets, and anticipated credit losses, including expected static pool losses,[9] ~~if applicable~~)[9a]

(4~~3~~) A sensitivity analysis or stress test showing the hypothetical effect on the fair value of ~~those interests~~any assets or liabilities that relate to continuing involvement of the transferor (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 (~~2~~3) 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

(5) Cash flows during the period between a nonconsolidated SPE and the transferor (including proceeds from new transfers, proceeds from collections reinvested in revolving-period transfers, purchases of previously transferred financial assets [or its underlying collateral], servicing fees, and cash flows received on the transferor's interests)

(6~~4~~) For the transferred financial ~~securitized~~ assets and any other financial assets that it manages together with them:~~[10]~~

(a) The total principal amount outstanding, the amount ~~portion~~ that has been derecognized, and the amount ~~portion~~ that continues to be recognized in each category reported in the statement of financial position, at the end of the period

(b) Delinquencies at the end of the period

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

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

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[6]~~Refer to footnote 11 to paragraph 19.~~

[7]If an entity has aggregated ~~made~~ multiple ~~securitizations~~ transfers ~~of the same major asset type~~ during a period in accordance with paragraph 16B, 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.

[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 financial assets.

[9a]The timing and amount of future cash flows for ~~retained~~ transferor's interests in ~~securitizations~~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~~securitized~~, because of the implicit credit or prepayment risk enhancement arising from the subordination.

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

s. Paragraph 27:

The nature and extent of supporting evidence required for an assertion in financial statements that transferred financial assets have been isolated—put presumptively beyond the reach of the transferor, any of its consolidated affiliates (that are not SPEs 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 where 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), whether the transferor is affiliated with the transferee, and other factors pertinent under applicable law. Derecognition ~~of transferred assets~~ for transfers of an individual financial asset in its entirety, a group of financial assets in their entirety, or a participating interest in an individual financial asset (which are referred to collectively in this Statement as *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 SPEs designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented **~~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)).

t. 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 with the assets and liabilities of the transferor or 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 it had no continuing involvement in the transferred financial assets or had experience with other transfers with the same facts and circumstances under similar applicable laws and regulations.

27B. 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.

u. 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~~ steps (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 for surrender of control.

v. Paragraphs 29–31 and the heading preceding them:

~~**Conditions That Constrain a Transferee**~~

~~29. Sale accounting is allowed under paragraph 9(b) only if each transferee 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. 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. 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.~~

~~30. However, some conditions do not constrain a transferee from pledging or exchanging the 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, because that right in itself does not enable the transferor to compel the transferee to sell the assets and the transferee would be in a position to receive the sum offered by exchanging the asset, albeit possibly from the transferor rather than the third party. Further examples of conditions that presumptively would not constrain a transferee 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 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.~~

w. Paragraphs 32 and 33, footnote 15, and the heading preceding them:

~~**Transferor's Rights or Obligations to Reacquire Transferred Assets**~~

~~32. Some rights or obligations to reacquire transferred assets 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~~

~~**freestanding call** option written by a transferee to the transferor benefits the transferor and, if the transferred assets are not readily obtainable in the marketplace, is likely to constrain a transferee because it might have to default if the call was exercised and it had exchanged or pledged the assets. A freestanding forward purchase-sale contract between the transferor and the transferee on transferred 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 rights to reacquire transferred assets that are readily obtainable presumptively do not constrain the transferee from exchanging or pledging them and thus do not preclude sale accounting under paragraph 9(b).~~

~~33. Other rights or obligations to reacquire transferred assets, regardless of whether they constrain the transferee, may result in the transferor's maintaining effective control over the transferred assets, as discussed in paragraphs 50–54, thus precluding sale accounting under paragraph 9(c)(2).[15]~~

~~[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.~~

x. Paragraph 34 and the heading preceding it:

~~**Conditions That Constrain a Holder of Beneficial Interests in a Qualifying SPE**~~

~~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.~~

y. Paragraphs 35, as amended, 36–39, 40, as amended, and 41–46, their related footnotes, and their related headings:

~~**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.~~

~~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.~~

~~[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]An 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.~~

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

Maintaining Effective Control over Transferred Financial Assets

To assess whether the transferor maintains effective control over the transferred financial assets, all involvements by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents shall be considered involvement by the transferor.

aa. 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 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 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.

bb. Paragraphs 50–53 and the heading preceding them:

Ability to Unilaterally Cause the Return of Specific Transferred Financial Assets

50. Some rights to reacquire transferred financial assets (or to acquire beneficial interests in transferred financial 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 financial assets through the **unilateral ability** to cause the return of specific transferred financial assets~~. Such rights preclude sale accounting~~ as described in ~~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~~ a transferred financial asset~~(s)~~ because the attached call gives the transferor the ability to unilaterally cause whoever holds that specific financial asset to return it. In contrast, a transfer~~s~~ of a financial asset~~s~~ subject to a call~~s~~ embedded by the issuers of the financial instruments, for example, callable bonds or prepayable mortgage loans, does 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.

~~51. If the transferee is a qualifying SPE, it has met the conditions in paragraph 35(d) and therefore must be constrained from choosing to exchange or pledge the transferred assets. In that circumstance, any call held by the transferor is effectively attached to the assets and could – depending on the price and other terms of the call – maintain the transferor's effective control over transferred 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 a transferred financial asset~~s~~ may provide ~~maintains~~ the transferor~~'s~~ with effective control over ~~those~~ that financial asset~~s~~ based on the~~if, under its~~ price and other terms~~,~~ of 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 provides the transferor with effective control~~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 a specific transferred financial asset~~s transferred to~~ ~~a qualifying SPE~~ at a price fixed at ~~their~~ its principal amount maintains the transferor's effective control over the financial asset~~s~~ subject to that call. Effective control over transferred financial 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 an ~~qualifying~~ SPE at a fixed price, then the transferor remains in effective control of the financial assets underlying those beneficial interests. Additionally, depending on the price and other terms of the call, a call that provides the transferor with the unilateral ability to cause an SPE to return to the transferor or otherwise dispose of specific transferred financial assets at will, for example, in response to the transferor's decision to exit a market or a particular activity, could provide the transferor with effective

control over the transferred financial assets. A cleanup call, however, is permitted as an exception to that general principle.

53. A right to reclaim specific transferred financial assets by paying their fair value when reclaimed generally does not maintain effective control~~, because it does not convey a more than trivial benefit to the transferor~~. However, a transferor may ~~has~~ maintain~~ed~~ effective control if it has such a right and also holds a ~~the~~ residual interest in the transferred financial assets. For example, if a transferor holds a residual interest in securitized financial assets and can reclaim ~~such~~the transferred financial assets at termination of the securitization ~~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.

cc. Paragraph 53A is added as follows:

The transferor must evaluate whether the combination of multiple arrangements maintains effective control of transferred financial assets. For example, if the transferor as the servicer for the transferred financial asset is empowered to offer the financial asset for sale and has the right of first refusal to purchase the financial asset, that combination of circumstances would place the transferor in a position to unilaterally cause the return of a specific transferred financial asset and thus maintain the transferor's effective control of the transferred financial asset.

dd. Paragraph 54:

A transferor that has a right to reacquire transferred financial assets from a transferee~~qualifying SPE~~ does not maintain effective control if the reclaimed financial assets would be randomly selected and the amount of the financial assets reacquired is sufficiently limited (paragraph 87(a)), because that would not be a right to reacquire *specific* financial assets. Nor does a transferor maintain effective control through an obligation to reacquire transferred financial assets ~~from a 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 transferee~~qualifying SPE~~ to repurchase that beneficial interest~~ (paragraph 44(b))~~, because the transferor could not cause that reacquisition *unilaterally*. Similarly, freestanding rights to reacquire transferred financial assets that are readily obtainable presumptively do not cause a transferor to maintain effective control. On the other hand, a **freestanding call** option written by a transferee to the transferor benefits the transferor and, if the transferred financial assets are not readily obtainable in the marketplace, is likely to cause a transferor to maintain effective control because the transferee might have to default if the call was exercised and the transferee had exchanged or pledged the financial assets. In much the same manner, 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 result in the transferor maintaining effective control as the transferee is constrained.

ee. Paragraphs 54A–54E and their related headings are added as follows:

Conditions That Constrain a Transferee

54A. A transferor maintains effective control over a transferred financial asset as described in paragraph 9(c)(3) if the transferee is constrained from pledging or exchanging the transferred financial asset it received and the constraint is not designed primarily to provide the transferee with a benefit. However, a transferor does not maintain effective control over a transferred financial asset if a constraint on the transferee's right to pledge or exchange the transferred financial asset is designed primarily to provide the transferee with a benefit. For example, in many securitization transactions, the transferee is restricted from pledging or exchanging the transferred financial asset. However, such restriction may exist primarily to benefit the transferee because it enhances the transferee's ability to market the issuance of securities backed by the transferred financial assets to prospective beneficial interest holders. Accordingly, the transferor does not maintain effective control over the transferred financial asset solely due to that constraint.

54B. Alternatively, a constraint on the transferee's right to pledge or exchange the transferred financial asset that is not designed primarily to provide the transferee with a benefit would provide the transferor with effective control over the transferred financial asset. For example, a provision that prohibits the transferee from selling or pledging a transferred loan receivable, which provides the transferor with the knowledge of who has the financial asset (a prerequisite to repurchasing the financial asset) and may block the financial asset from finding its way into the hands of a competitor, provides no benefit to the transferee. The transferee's ability to receive the economic benefits of the transferred financial asset (that is, to collect cash flows from the transferred financial asset) does not result in the transferee receiving a benefit from the constraint.

54C. Some conditions do not constrain a transferee from pledging or exchanging the financial asset and, therefore, do not provide the transferor with effective control over the transferred financial asset. 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 the right in itself does not enable the transferor to compel the transferee to sell the 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.

54D. Judgment is required to assess whether a particular condition results in a constraint and, if so, whether that constraint is designed primarily to provide a benefit to the transferee. Judgment also is required in assessing the significance of the benefit and whether the constraint provides the transferor with the ability to effectively control the transferred financial asset. It is necessary to consider the overall effect of related rights and obligations in assessing such matters as whether (a) a transferee is constrained, (b) the transferee receives a benefit from such constraint, and (c) the transferor maintains effective control over the transferred financial assets. For example, a prohibition on sale to the transferor's competitor would be a constraint if that competitor was the only potential willing buyer other than the transferor.

Arrangements to Reacquire Transferred Financial Assets

54E. A transferor maintains effective control over the transferred financial asset as described in paragraph 9(c)(4) 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 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.

ff. 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 the transferor's regaining control of transferred financial assets subsequent to 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 a change, unless it arises solely from (a) ~~either~~ the initial application of this Statement, (b) consolidation of an entity involved in the transfer at a subsequent date (see paragraph 55A), or (c) 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), 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 paragraph 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 of the former transferee(s)~~in those assets (paragraph 38)~~. 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.

gg. 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.

hh. 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~~.

ii. Paragraph 57, as amended:

Company A transfers ~~sells~~ loans in their entirety to an SPE with a fair value of $1,100 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	~~$1,100~~ $1,030

Gain on Sale

Net proceeds	~~$1,100~~ $1,030
Carrying amount of loans sold	1,000
Gain on sale	~~$ 100~~ $30

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.

jj. 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 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.~~

kk. 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 asset 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 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 transferor	110	10	100
Total	$1,100	100	$1,000

Gain on Sale

Net proceeds	$990
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.

ll. Paragraphs 61–63, as amended, and 62A, as added:

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 a financial asset, it would recognize a servicing asset or servicing liability that qualifies for recognition, if any, related to the participating interest sold, but would not recognize a separate servicing asset or servicing liability related to the participating interest that it continues to hold.

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 transfer of a servicer's individual financial asset in its entirety, a group of the servicer's financial assets in their entirety, or a participating interest in a servicer's individual 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 (b~~c~~) 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 in a guaranteed mortgage securitization, retains all of 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.
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).

mm. 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 transfers ~~sells~~ the loans in their entirety 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~~ 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.

nn. 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~~

oo. 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.~~*

pp. 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 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.~~

~~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.~~

qq. Paragraph 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.

rr. Paragraph 75:

Beneficial interests in the 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 SPE.

ss. Paragraph 76, as amended:

Pass-through, pay-through, and revolving-period securitizations that meet the criteria in paragraph 9 qualify for sale accounting under this Statement. 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.

tt. 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. To achieve sale accounting for ~~R~~revolving-period securitizations, a transferor 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.~~

uu. Paragraphs 80–83, as amended, and 84, 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 SPEs 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 paragraph 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, if it failed, transfers financial assets to an SPE~~special purpose trust~~ in exchange for cash. The SPE~~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 SPEs 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 an SPE in exchange for cash and beneficial interests in the transferred financial assets. That SPE~~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 received ~~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 SPE~~trust~~. The senior beneficial~~commercial paper~~ interests (the 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 SPEs 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 SPEs 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 financial assets to a consolidated SPE ~~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 SPEs 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 SPE~~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 SPEs 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 SPE~~special-purpose corporation~~ transfers ~~the~~ an individual financial asset~~s~~ in its entirety, a group of financial assets in their entirety, or a participating interest in an individual financial asset to a trust or other legal vehicle with a sufficient increase in the credit or yield protection on the second transfer (provided by a junior beneficial transferor interest's ~~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 SPE~~special-purpose corporation~~.
c. However, the SPE~~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 SPEs 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 SPE involved in a transfer must be evaluated under the applicable consolidation 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 Federal Deposit Insurance Corporation (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 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.

vv. Paragraphs 85–87, as amended, and 88:

85. Many transfers of financial assets 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 (paragraphs 9(c)(2) and ~~51~~50–54).

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, 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, 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, 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 are recognized because the transferor now can unilaterally cause the transferee ~~qualifying SPE~~ to return those specific financial assets and, therefore, the transferor once again has effective control over those transferred financial assets (paragraph 55).

ww. 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 and 13, if appropriate.

xx. 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.[21b] 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. 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		

[21b]See footnote 18a.

yy. Paragraphs 92 and 93:

> 92. In some securities lending transactions, the criteria 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 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.

zz. Paragraphs 97–101:

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 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]~~transferee 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 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 unless the constraint is designed primarily to provide the transferee with a benefit.

aaa. 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.

bbb. 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 an~~undivided~~ interest~~s~~ in the loan to other entities.

ccc. Paragraph 106:

If the loan participation agreement transfers a participating interest in a 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 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 transferees from pledging or exchanging their ~~participations~~participating interest~~, the transferor presumptively receives a more than trivial benefit~~, the transferor generally has not relinquished control over the participating interest unless the constraint meets the criteria in paragraph 9(c)(3)~~loan,~~ and shall account for the transfer~~s~~ as a secured borrowing~~s~~.

ddd. Paragraph 112:

Factoring arrangements are a means of discounting accounts receivable on a nonrecourse, notification basis. Accounts receivable are sold in their entirety 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 in paragraph 9 shall be accounted for as sales of financial assets because the transferor surrenders control over the receivables to the factor.

eee. Paragraph 113:

In a transfer of a receivable~~s~~ in its entirety, a group of receivables in their entirety, or a participating interest in an individual receivable with recourse, the transferor provides the transferee with full or limited recourse. A transfer of a portion of a receivable that does not meet the requirements of a participating interest 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 SPEs 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 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 in paragraph 9 are met. Otherwise, a transfer of receivables with recourse shall be accounted for as a secured borrowing.

fff. Paragraph 113A and the heading preceding it are added as follows:

Transfers of a Senior Interest in Receivables

In other cases, a transferor may transfer a portion of an individual receivable or a group of receivables that represent a senior interest in an individual receivable or a group of receivables. In those cases, the transferors would account for the transfer as a secured borrowing because the senior interest in the receivables does not meet the requirements to be a participating interest.

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

hhh. 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 received by an SPE~~to 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 (or in a series of beneficial interests in transferred financial assets within an ~~qualifying~~ SPE), 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. Examples of continuing involvement include, but are not limited to, servicing arrangements, recourse or guarantee arrangements, agreements to purchase or redeem transferred financial assets, derivative instruments related to the transferred financial assets, implicit commitments to provide financial support, pledges of collateral, or the transferor's beneficial interests.

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. It represents a proportionate ownership interest in an entire individual financial asset other than an equity instrument, a derivative financial instrument, or a hybrid financial instrument with an embedded derivative that is not clearly and closely related as described in Statement 133.
b. All cash flows received from the asset are divided among the participating interests (including any interest retained by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents) in proportion to the share of ownership represented by each. Cash flows allocated to a servicer as compensation for servicing activities, if any, shall not be included in that determination. The transferor's ownership shares must remain pro rata over the life of the original financial asset. Participating interests may be further apportioned by the transferor as long as the resulting portions meet the definition of a participating interest.
c. The rights of each participating interest holder (including the transferor if it retains a participating interest) have the same priority, and that priority does not change in the event of bankruptcy or other receivership of the transferor, the original debtor, or any participating interest holder. Participating interest holders have no recourse, other than standard representations and warranties, to the transferor (or its consolidated affiliates included in the financial statements being presented or agents) or to each other, and no participating interest holder is subordinated to another. That is, no participating interest holder is entitled to

receive cash before any other participating interest holder in its role as a participating interest holder.

d. No party has the right 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.

Transferee

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

Transferor

An entity that transfers an individual financial asset in its entirety, ~~a portion of a financial asset, or~~ a group of financial assets in their entirety, or a participating interest in an individual financial asset 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 applied to transfers occurring on or after the beginning of a reporting entity's first fiscal year that begins after November 15, 2009. Earlier application is prohibited.

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

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

Appendix A

BACKGROUND INFORMATION AND BASIS FOR CONCLUSIONS

CONTENTS

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 proposed 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 (SPE) 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 SPEs because of two main factors. 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 SPE. Statement 140 also established the isolation of transferred financial assets as a condition for derecognition of those assets. However, Statement 140 did not specify the powers of a qualifying SPE to retire and reissue beneficial interests, and in 2002, the Emerging Issues Task Force (EITF) attempted to clarify those powers. 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," but the EITF did not reach a consensus on that Issue. Second, FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities,* did not apply to interests in qualifying SPEs, except in certain limited circumstances. Because a qualifying SPE was generally exempt from consolidation, the Board decided that it was important to clarify its characteristics. As the project progressed, the Board decided that other aspects of Statement 140 required clarification or improvement, including issues related to isolation and the initial measurement of interests in transferred financial assets that continue to be held by a transferor.

A3. In June 2003, the Board issued the FASB Exposure Draft, *Qualifying Special-Purpose Entities and Isolation of Transferred Assets*. There were 52 responses 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 those redeliberations, 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.

A4. In addition, the Board decided to solicit information about isolation issues, including the effect of setoff rights on isolation. In April 2004, the staff posted for public comment an FASB Staff Request for Information about the isolation of transferred financial assets.

The staff received 33 comment letters from law firms, financial institutions, trade associations, and regulators of financial institutions. 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 provisions of the 2003 Exposure Draft on qualifying SPEs and isolation of transferred financial assets, the Board decided it needed additional input from constituents and that such input could be obtained by issuing a revised FASB Exposure Draft, *Accounting for Transfers of Financial Assets,* which was issued 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. After the issuance of that Exposure Draft, the Board continued to receive questions about the permitted activities of a qualifying SPE, including requests from constituents to address questions related to qualifying SPEs used in commercial and residential mortgage loan securitizations. The FASB also was asked whether the status of a qualifying SPE could be retained if the underlying loans were modified before an event of default. Those modifications may occur prior to default if unexpected events require loans to be modified when default is imminent or reasonably foreseeable to protect and/or enhance the cash flows in the SPE available to beneficial interest holders. This proposed Statement is the result of deliberations on comments received on the 2005 Exposure Draft on accounting for transfers of financial assets, subsequent constituent inquiries (including financial statement user requests for greater transparency), and market conditions over the past three years including, but not limited to, the impact of the recent credit crisis in the United States.

A6. In addition to the 2003 and 2005 Exposure Drafts, the Board decided to separately address related issues involving accounting for hybrid financial instruments and accounting for servicing of financial assets. In August 2005, the Board issued two other Exposure Drafts that proposed amendments to Statement 140: *Accounting for Certain Hybrid Financial Instruments* and *Accounting for Servicing of Financial Assets*. After redeliberating certain issues related to hybrid financial instruments and servicing of financial assets, the Board issued FASB Statements No. 155, *Accounting for Certain Hybrid Financial Instruments,* and No. 156, *Accounting for Servicing of Financial Assets.* During deliberations on this project, the Board also issued three FASB Staff Positions (FSPs) to address practice issues related to the application of Statement 140: 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*.

A7. During redeliberations on the 2005 Exposure Draft on accounting for transfers of financial assets, the Board learned that financial statement users and other constituents believed 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. Some users noted that they believed that derecognition should not be permitted if a transferor has any continuing involvement in the transferred financial assets.

Amendments to Statement 140

Amendments Related to the Isolation of Transferred Financial Assets

A8. In the past few years, the Securities and Exchange Commission (SEC) staff, auditors, and other constituents have raised concerns about the accounting for certain transfers. In particular, the SEC staff objected to certain transfers of undivided interests in pools of financial assets that were being reported as sales because significant credit support also was provided by affiliates of the transferors. The SEC staff 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 contracts continued to be in the custody of the transferor and/or consolidated affiliates included in the financial statements being presented. The Board decided it was necessary to simplify and clarify the guidance on isolation to improve comparability and consistency in the application of the isolation guidance in paragraph 9(a) of Statement 140 and related implementation guidance.

A9. 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 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, which states:

> Derecognition of transferred assets is appropriate only if the available evidence provides reasonable assurance that the transferred assets would be beyond the reach of the powers of a bankruptcy trustee or other receiver for the transferor or any **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.

A10. In developing Statements 125 and 140, the Board concluded that the isolation condition in paragraph 9(a) of Statement 140 is an important consideration in deciding whether to derecognize a financial asset. The Board acknowledged that a transferor must rely on a legal analysis of what would happen if the transferor enters bankruptcy or receivership, and in some cases, the transferor may rely on the opinion of an attorney who may not be familiar with U.S. generally accepted accounting principles (GAAP). Several Board members observed that attorneys, including attorneys who commented on the 2003 and 2005 Exposure Drafts on qualifying SPEs 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 proposed 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 based on 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.

A11. The Board concluded that under U.S. bankruptcy law, a true sale opinion and, in the case of transfers to affiliated entities, a nonconsolidation opinion would often be required 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 agreed that other jurisdictions would require a legal analysis, similar to a true sale opinion, to support a conclusion about whether a transferred financial asset has been isolated. The Board decided that a legal opinion should not be required if a transferor could determine through other means what the legal conclusion would be if a legal opinion was requested. The Board acknowledged that the additional implementation guidance in paragraph 27A of Statement 140, as amended by this proposed Statement, would only be applicable for transferors under the jurisdiction of U.S. bankruptcy law. However, the Board believes that it would reduce practice issues for those transferors and provide an example that may be used by analogy by transferors under other legal jurisdictions.

A12. In addition, the Board decided to clarify that any arrangements made contemporaneously with, or in contemplation of a transfer of financial assets should be considered even if those arrangements were not entered into at the time of the transfer.

A13. During the deliberations before the 2005 Exposure Draft on accounting for transfers of financial assets, the Board also considered the issue of setoff rights before concluding that the isolation requirement should continue to be based on a legal analysis. A setoff 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 Request for Information, and rating agencies told the Board that the existence of setoff rights are 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 setoff right involving a financial asset that had been transferred. In the event of the bankruptcy of the transferor, the transferee may only have an unsecured claim against the transferor for its share of the amount set off.

A14. Several Board members believed that setoff rights involving a transferred financial asset should be severed to meet the isolation requirement. However, the Board learned that it may not be possible to sever setoff rights related to transferred financial assets. For example, certain consumer protection rules prevent consumers from waiving their ability to exercise setoff 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 setoff 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 setoff 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 setoff risks are assessed and priced into transactions like other dilutive risks, such as warranties and returns. The Board ultimately decided that setoff rights would not be an impediment to meeting the isolation requirement.

A15. Following the 2005 Exposure Draft on accounting for transfers of financial assets, the Board considered but later rejected an alternative that would require that the isolation analysis be performed based upon 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 it would not reduce variance in practice, but could actually increase variance in practice since 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.

A16. 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 completed jointly with the International Accounting Standards Board (IASB). The Board's Memorandum of Understanding indicates that after the Boards complete their separate improvement projects, they will develop a strategy to develop a common standard.

Amendments Related to Qualifying SPEs

A17. The Board developed the conditions for qualifying SPEs primarily to permit derecognition of assets in certain transactions in which the transferee is a passive entity that cannot pledge or exchange the transferred financial assets. The Board concluded in Statement 125, and reaffirmed in Statement 140, that a transfer of financial assets to a passive pass-through entity that cannot pledge or exchange the transferred financial assets should nevertheless generally permit the transferor 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 SPE that were designed to ensure that consideration of 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 SPE 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 SPEs from the scope of FASB Interpretation No. 46, *Consolidation of Variable Interest Entities,* and Interpretation 46(R) for the same reasons.

A18. At the time it developed the conditions for qualifying SPEs in Statements 125 and 140, the Board believed that transferee entities used in securitizations were largely 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 for a qualifying SPE specified in paragraph 35(b) of Statement 140 that require a qualifying SPE'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 Board has since decided to remove the concept of a qualifying SPE in its entirety from this proposed Statement. The following were some of the issues that raised questions about whether the passivity conditions required for a qualifying SPE are being met and enforced in practice:

a. Rollovers of beneficial interests
b. Servicer discretion practice issues
c. Constituent and SEC staff inquiries about whether a qualifying SPE could maintain its qualifying status when responding to unexpected events, such as the recent credit crisis.

Rollovers of Beneficial Interests

A19. The Board began this project because of questions raised about whether the restrictive conditions for a qualifying SPE (a) require that the terms of beneficial interests to be issued be specified at inception of the entity or (b) permit the qualifying SPE (or its designee or agent) to establish the terms of replacement beneficial interests. The Board questioned whether an existing qualifying SPE (or its designee or agent) that determines the terms of beneficial interests issued after the inception of the qualifying SPE satisfies the passivity requirements in Statement 140.

A20. The Board learned that qualifying SPEs 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 SPE 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, further, whether a qualifying SPE should continue to be generally excluded from the scope of Interpretation 46(R) and other consolidation guidance.

A21. In the 2005 Exposure Draft on accounting for transfers of financial assets, the Board proposed to address the issue of rollovers by requiring that no party may have two or more involvements with a qualifying SPE that provide that party with the opportunity to obtain a more-than-trivial incremental 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 believed it could not be operationalized without extensive additional guidance and would be difficult to audit.

Servicer Discretion

A22. 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 SPE. They requested clarification about the requirement that the activities of a qualifying SPE be significantly limited and entirely specified in the legal documents that establish the qualifying SPE or create the beneficial interests in the transferred financial assets held. 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 centered on whether certain types of transactions met the criteria of a qualifying SPE and how much discretion a servicer of a qualifying SPE should be allowed when responding to events that are outside the control of the transferor.

A23. The staff and some Board members met with constituents and concluded that, in practice, many qualifying SPEs 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 in the event of unforeseen events or to engage in activities that reach beyond the requirement in Statement 140 to be significantly limited for qualifying SPEs. Some parties indicated that the long-term nature of many of these transactions makes it impractical to predict all the possible events that may require a response from a servicer 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 SPE for many types of financial assets, most notably financial assets with longer terms.

Recent Credit Crisis in the United States

A24. 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 engaged a wide range of experts in a discussion of current issues encountered by industry participants in connection with modifications of securitized mortgage loans held in qualifying SPEs. It was designed to determine whether additional guidance from regulators or accounting standard setters would be necessary. 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 SPE 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.

A25. The proposed loan modifications at issue included those that were being made, or that 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 payment obligations 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 regarding when an entity may modify a loan without impacting qualifying SPE status since 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 SPE's legal documents. Some participants also raised questions about the accounting for loan modifications when default is imminent or reasonably foreseeable. Following the forum, the Board decided to consider that issue as part of its ongoing project on Statement 140.

Removal of the Qualifying SPE Concept

A26. Board members believe that the range of financial assets being securitized and the complexity of securitization structures and arrangements have resulted in the qualifying SPE criteria being stretched in some cases beyond the intent and requirements of Statement 140, thus effectively rendering the criteria no longer operational in practice. The Board considered an approach that would have strengthened the passivity requirement of the permitted assets of a qualifying SPE; however, after discussing this possible approach with constituents, Board members concluded that there are few classes of financial assets that are truly passive as envisioned in the qualifying SPE concept. As a result, the Board decided to remove the concept of a qualifying SPE from Statement 140.

A27. As a result of its decision to remove the concept of the qualifying SPE from Statement 140, the Board decided to remove the scope exception for qualifying SPEs from consolidation guidance, including the guidance in Interpretation 46(R). The Board considered the potential impact of the elimination of the qualifying SPE concept on the application of Interpretation 46(R) to formerly qualifying SPEs and noted that the elimination would put additional pressure on the framework of the 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).

A28. Some users of financial statements, including members of the Investors Technical Advisory Committee, recommended a no-continuing-involvement model as an alternative. As discussed in paragraph A7, these users believe that derecognition should not be permitted if a transferor has any continuing involvement in the transferred financial assets. However, the Board was concerned that a no-continuing-involvement-model would not properly reflect the economics of many simple transfers.

A29. The Board also considered a linked presentation model, similar to the model being considered as part of the research project on derecognition of financial assets. In a linked presentation model, the assets remain on the face of an entity's statement of financial position, but any liability that is satisfied by those assets would be shown as a deduction from the related assets on the face of the statement of financial position with a subtotal for a net amount. When the Board added the related project to amend Interpretation 46(R), it considered whether the scope of linked presentation should be extended. The Board decided that the linked presentation model cannot be considered only for a subset of assets and liabilities but must be developed for all financial and nonfinancial assets that would satisfy related liabilities. The Board concluded, however, that extending the scope of linked presentation to a much broader population of assets and liabilities, including those that are nonfinancial, is a significant change that would be more appropriately developed as part of the joint projects with the IASB on derecognition and/or financial statement presentation. Further, the Board decided that it would need to address significant issues related to linked presentation that could not be completed in the short term, such as issues related to measurement of the linked assets and liabilities and determining which assets and liabilities would be shown as linked. Several Board members concluded that the subsequent measurement attribute of assets and liabilities shown as linked should be fair value and that the application of fair value to a broad spectrum of assets and liabilities needed further analysis. Consequently, the Board decided not to pursue a linked presentation model at this time because of the narrow scope and short-term nature of this project. However, the Board decided to require disclosure in the notes to the financial statements of assets with cash flows restricted to satisfy a specific obligation in the notes to the financial statements.

Removal of Exception for Guaranteed Mortgage Securitizations

A30. FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* amended FASB Statement No. 65, *Accounting for Certain Mortgage Banking Activities,* to require that a securitization of a mortgage loan held for sale be accounted for as a sale of the mortgage loan and a purchase of a mortgage-backed security, classified as a trading security at fair value if the enterprise commits to sell the security before or during the securitization process, even if the transaction does not meet the requirements for sale accounting. Statement 140, as amended by Statement 156, requires that a transferor recognize a servicing asset or servicing liability at fair value if the transferor transfers mortgage loans to a qualifying SPE in a guaranteed mortgage securitization and retains all the resulting securities, which must be classified as either available for sale or trading securities.

A31. The Board questioned whether it was appropriate to reclassify a financial asset as a security, which could result in a change in the measurement attribute for financial assets when a transferor has not met the requirements for sale accounting. Also, 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. Accordingly, the Board decided to delete the exception for guaranteed mortgage securitizations. The Board does not believe that it is appropriate to provide an exception for only one asset type since that would enable a transferor to recognize a gain or loss when the transferor has not met the requirements for sale accounting. The Board notes that the decision to not permit a change in the measurement attribute following a guaranteed mortgage securitization is consistent with the Board's decisions to require fair value measurement for new assets and liabilities received as proceeds and to not permit remeasurement for participating interests that continue to be held by the transferor (see paragraphs A38–A40). Further, the Board noted that the fair value option provided by 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. Finally, the Board concluded that it is not appropriate for a transferor to separately recognize a servicing asset or servicing liability when the transferor has not met the requirements for sale accounting.

A32. As a result of the Board's decision to remove these exceptions for a guaranteed mortgage securitization, a guaranteed mortgage securitization will have the same accounting rules as any other transfer of financial assets. As such, a guaranteed mortgage securitization may still be treated as a sale if the securitization meets the requirements for sale accounting in paragraph 9 of Statement 140, as amended by this proposed Statement.

Amendments Related to the Application of Paragraph 9(b)

A33. The 2003 Exposure Draft on qualifying SPEs and isolation of transferred financial assets would have required that a two-step transfer of financial assets use a qualifying SPE as the second and final step if the transfer results in the issuance of beneficial interests (whether in the form of securities or undivided interests) to meet the condition in paragraph 9(b) of Statement 140. The Board decided to address practices that had developed after the issuance of Statement 140 that caused some transferors to believe that a transfer from a bankruptcy-remote entity that takes the form of undivided interests could meet the condition in paragraph 9(b); however, a transfer from a bankruptcy-remote entity that takes the form of beneficial interests would not meet the condition in paragraph 9(b) unless a qualifying SPE was used. Some constituents argued that whether a transfer creates beneficial interests or undivided interests has significance. They also contended that a transfer of an undivided interest meets the condition in paragraph 9(b) because an undivided interest is essentially the sale of a portion of a financial asset, and parties that receive an undivided interest can pledge or sell the undivided interests without constraint.

A34. The Board considered constituents' comments and concluded that undivided interests and beneficial interests are not sufficiently different to warrant different accounting. Because those terms are used in different ways in practice, the Board decided that this proposed Statement should clarify their definitions. The term *beneficial interest* has been redefined for purposes of this proposed Statement to mean the right to receive specified cash inflows received by an SPE, 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.

A35. The Board recognized that Statement 140 used the term *undivided interest* inconsistently and that many constituents believed 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 that Statement. To eliminate the inconsistent use of the term *undivided interest,* the Board decided to delete the term *undivided interest* and to use the term *participating interest* to describe the transfer of a portion of a financial asset. The Board established the definition of a *participating interest* and guidance with respect to whether a transfer in the form of a participating interest meets the derecognition criteria in paragraph 9. See paragraphs A38–A40 for more information on participating interests.

A36. As noted above, the Board decided to eliminate the concept of a qualifying SPE and the exception for qualifying SPEs in paragraph 9(b) of Statement 140. The Board then debated whether the ability of a transferee to pledge and 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. However, the Board concluded that in cases where a financial asset is transferred to a securitization entity, a constraint on the ability of the transferee to sell or exchange its assets is usually, but not always, necessary if the transferee intends to issue beneficial interests. Accordingly, such a constraint would not indicate that the transferor has maintained effective control. However, in other cases, a constraint on the ability of the transferee to sell or exchange its assets may be designed to primarily benefit the transferor and may indicate that the transferor has maintained effective control. As a result, the Board decided that it was more appropriate to remove paragraph 9(b) from Statement 140 in its entirety and to consider the impact of constraints on the transferee under paragraph 9(c) of this proposed Statement, which addresses effective control.

A37. The implementation guidance in Statement 140 requires that the impact of certain forms of continuing involvement, such as a transferor's rights or obligations to reacquire transferred financial assets, be considered when assessing whether a transferor meets the conditions for sale accounting described in paragraph 9(b) of that Statement. The Board concluded that some forms of continuing involvement also need to be evaluated when assessing whether a transferor maintains control over the transferred financial assets as described in paragraph 9(c) of Statement 140. Therefore, the Board has included that guidance in paragraph 9(c) of Statement 140 and related implementation guidance, as amended by this proposed Statement, with some modifications. In addition, the Board decided to clarify that any arrangements made contemporaneously with, or in contemplation of, a transfer of financial assets should be considered even if those arrangements were not entered into at the time of the transfer.

Amendments Related to Transfers of Portions of Financial Assets

A38. Board members who expressed reservations about relying solely on an attorney's legal assessment do not believe that a financial asset has been isolated from the transferor unless the entire financial asset has first been placed in an SPE or otherwise segregated from the transferor. Other Board members preferred to rely solely on the contract terms and a legal assessment to determine whether a portion of a financial asset is isolated and to rely on investor demands and the application of paragraph 9(b) of Statement 140 to determine whether a transfer of the entire financial asset to a qualifying SPE would be necessary. The 2005 Exposure Draft on accounting for transfers of financial assets had limited sale accounting for transfers of a portion or portions of a financial asset as a sale to transfers of a portion or portions of a financial asset that meets the requirements of a participating interest. If the transfer of a portion or portions of a financial asset did not meet the requirements of a participating interest, sale accounting could be achieved only by transferring the entire financial asset or group of financial assets to a qualifying SPE or other entity that is not consolidated with the transferor, and the entire transferred financial asset or group of financial assets must meet the conditions of paragraph 9 of Statement 140, as amended by that proposed Statement.

A39. A significant number of the respondents to the 2005 Exposure Draft on accounting for transfers of financial assets disagreed with the proposed participating interest requirement because a qualifying SPE would be required to account for the transfer as a sale if the portion of financial assets did not meet the requirements to be a participating interest. Such concerns have been mitigated by the Board's decision to remove the qualifying SPE concept from Statement 140. After discussing those concerns and its decision to remove the concept of a qualifying SPE, the Board decided to require that the entire original financial asset first be transferred to an entity for which the transferor does not maintain a controlling financial interest unless the portions transferred meet the definition of a participating interest (see paragraph 8B of Statement 140, as amended by this proposed Statement).

A40. During the redeliberations following the 2005 Exposure Draft on accounting for transfers of financial assets, the Board considered constituents' comments and decided to reaffirm its decision on the definition of a participating interest. Constituents also commented that the recourse provision in the participating interest definition of that Exposure Draft inappropriately included standard representations and warranties. In its redeliberations, the Board decided to specifically exclude standard representations and warranties when determining if the participating interest holder has recourse to the transferor. However, the Board decided that it was necessary to provide specific guidance on the definition of a portion of a financial asset to (a) improve comparability in reporting similar transactions, (b) reduce the opportunity for form-over-substance structures, and (c) resolve concerns that a transferor has retained control over derecognized portions of financial assets.

Amendments Related to Initial Measurement of Transferred Financial Assets

Measurement of a Transferor's Beneficial Interest

A41. Statement 140 requires beneficial interests that continue to be held by a transferor to be measured by allocating the carrying amount of the transferred financial assets between the financial assets sold and the financial assets retained based on 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 it asserts that surrender of control has not occurred for the retained beneficial interests because those interests never left the possession of the transferor.

A42. After the Board's decisions to amend Statement 140's requirements applicable to transfers of portions of financial assets, the Board reconsidered the nature of a transferor's beneficial interest in transferred financial assets. This proposed Statement would require a transferor to transfer an individual financial asset in its entirety, a group of financial assets in their entirety, or a participating interest in an individual financial asset to apply the guidance for sale accounting in paragraph 9 of Statement 140, as amended by this proposed Statement. The Board concluded that any beneficial interest or other asset or liability that the transferor receives from a transfer that qualifies as a sale is proceeds of the sale and represents a new asset or liability to the transferor. Accordingly, the Board concluded that a beneficial interest issued by an entity that the transferor does not consolidate should be initially measured the same way as other assets received by a transferor from an entity that the transferor does not consolidate. The Board, therefore, decided to require that a transferor's beneficial interests in transferred financial assets be initially measured at fair value.

Measurement of a Transferor's Participating Interest

A43. In considering the measurement of a transferor's participating interest, the Board concluded that a transferor's participating interest has not been transferred. Rather, only the participating interest sold to third parties has been transferred and, therefore, the transferor has surrendered control over only that transferred interest. Consequently, the Board decided to require that participating interests be initially measured by allocating the carrying amount of the original financial asset between the participating interests sold and the transferor's participating interest based on relative fair value.

Amendments Related to the Fair Value Practicability Exception

A44. As discussed in the basis for conclusions in 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 for practical reasons. Alternatively, the Board indicated that issues related to some practicability exceptions would be addressed in other agenda projects.

A45. 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

A46. In developing the incremental disclosures included in this proposed Statement, the Board noted that existing U.S. GAAP already requires numerous disclosures related to transfers of financial assets, risks and uncertainties, credit concentrations, derivatives, and assets measured at fair value. However, the Board concluded that some of these 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 made by financial statement users to develop the proposed 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.

A47. Financial statement users told the Board that they need additional information about transferred financial assets when the transferor has continuing involvement in the transferred financial assets, regardless of whether the transferor accounts for the transfer of financial assets as a sale or as a secured borrowing. Financial statement users also told the Board that enhanced disclosures urgently are needed to improve transparency about the extent of continuing involvement a transferor has in transferred financial assets.

A48. The Board agreed with those views and expects that the incremental disclosures will provide increased transparency for transferred financial assets, in particular, those that involve SPEs. The Board decided that it was important to first develop overall objectives for the disclosures on transferred financial assets and then to enhance the existing required disclosures in Statement 140 because it is not possible to develop specific disclosures that would anticipate all existing and future transactions. The Board also decided that the disclosure objectives should encompass the existing disclosures, such as the servicing disclosures that were recently enhanced by Statement 156. The Board concluded that the disclosure objectives would provide preparers with the guidance necessary to provide financial statement users with an understanding of:

a. A transferor’s continuing involvement in financial assets that it has transferred to an SPE
b. The nature of any restriction on assets reported by a transferor in its statement of financial position, including the carrying amounts of such assets

c. How servicing assets and servicing liabilities are reported by a transferor under Statement 140, as amended by this proposed Statement
d. How a transfer of financial assets affects an entity's financial position, financial performance, and cash flows.

A49. Footnote 10 to paragraph 17(i)(4) of Statement 140 provides an exception from the disclosures required by that paragraph if a transferor's only continuing involvement is servicing the transferred financial assets. Based on 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.

A50. Paragraph 17(h)(2) of Statement 140 requires a description of the transferor's continuing involvement and provides examples of continuing involvement. It is only applicable to securitizations completed in the periods presented. As a result of the Board's decision to amend paragraph 17(i) 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 based on examples of what constitutes continuing involvement that were already provided in Statement 140 and in the FASB Special Report, *A Guide to Implementation of Statement 140 on Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*.

A51. The Board decided to include an aggregation principle in the amendment to the disclosure requirements of Statement 140. 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. The Board noted that since the issuance of Statement 140, it has issued FSP SOP 94-6-1, *Terms of Loan Products That May Give Rise to a Concentration of Credit Risk*. The Board decided that FSP SOP 94-6-1 already should be considered in providing the disclosures that would be required by this proposed Statement.

A52. 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 SPE concept and the related exception from consolidation guidance. The Board noted that this proposed amendment would require additional disclosures if the transferred financial assets involve an SPE that is considered to be a variable interest entity under Interpretation 46(R). Accordingly, the Board considered the proposed disclosure enhancements in Interpretation 46(R) and decided that both Statement 140 and Interpretation 46(R) would require enhanced disclosures for SPEs.

Effective Date and Transition

A53. The Board concluded that the requirements of this proposed Statement should be effective as soon as reasonably possible for the following reasons:

a. Given the current economic environment, 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.
b. There is significant diversity in practice in applying Statement 140 to transfers of financial assets.
c. Constituents raise frequent application questions relating to Statement 140.

The Board decided that it is important to establish the same effective date for both this proposed Statement and the proposed Statement to amend Interpretation 46(R) because many transactions would be affected by both proposed Statements.

A54. The Board considered both a single effective date that would require this proposed Statement to be applied as of the beginning of each reporting entity's first fiscal year that begins after November 15, 2009, on a prospective basis, except that all existing qualifying SPEs would need to be evaluated for consolidation as of the effective date and a dual effective date that would require this proposed Statement to be applied prospectively in fiscal years beginning after November 15, 2008, but that would delay evaluation of existing qualifying SPEs for consolidation until fiscal years beginning after November 15, 2009.

A55. The Board recognizes that the removal of the qualifying SPE 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 SPE scope exception and implement any necessary changes, including potential changes to regulatory capital requirements.

A56. The Board originally considered whether this proposed Statement should be effective for fiscal years beginning after November 15, 2008. However, in order to have sufficient time to adequately discuss the proposed amendments with preparers, regulators, auditors, and financial statement users, the Board did not issue this proposed Statement until September 2008. The Board noted that preparers, regulators, auditors, and financial statement users need adequate time to consider and implement the proposed amendments and specifically discussed the impact 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. However, if the effective date is not until 2010, they believe that additional disclosures should be required in the interim. As a result, the Board decided that this proposed Statement should be applied to transfers occurring on or after the beginning of a reporting entity's first fiscal year that begins after November 15, 2009. Additionally, all existing qualifying SPEs would need to be evaluated for consolidation by all reporting entities as of the effective date.

A57. The transaction-based prospective approach used in this proposed Statement is similar to the approach used when Statement 140 was issued and was adopted in this proposed 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. Although the Board realizes that some constituents may request additional time, the Board decided that for the reasons cited in paragraph A53 of this proposed Statement, the proposed amendments should become effective as soon as reasonably possible.

A58. In addition, the Board decided to separately issue an FSP that would amend and enhance the disclosures required by Statement 140 until this proposed Statement becomes effective. The purpose of a disclosure-only FSP is to expeditiously meet financial statement user needs for greater transparency of off-balance sheet transactions as well as to provide adequate time for preparers and others to consider and implement the other proposed amendments to Statement 140 and Interpretation 46(R). Accordingly, the Board believes that the proposed FSP should be effective no later than the first interim reporting period in fiscal years beginning after November 15, 2008, with early application encouraged.

Benefits and Costs

A59. The mission of the FASB is to establish and improve standards of financial accounting and reporting to provide information that is useful to users of financial statements (present and potential investors, creditors, and other capital market participants) in making rational investment, credit, and similar resource allocation decisions. In fulfilling that mission, the Board endeavors to determine that a standard will fill a significant need and that the costs imposed to apply that standard, as compared with other alternatives, are justified in relation to the overall benefits of the resulting information. Although the costs to implement a new standard may not be borne evenly, users of financial information benefit from improvements in financial reporting, thereby facilitating the functioning of markets for capital and credit and the efficient allocation of resources in the economy.

A60. The most important benefit of this proposed Statement would be to provide users of financial statements 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 users of financial statements have told the FASB that enhancements to the information required by Statement 140 are urgently needed to capture the economic substance of the transfers, and some recommended that transferred financial assets remain on the balance sheet if a transferor has any continuing involvement in the transferred financial assets. They also have told the Board that they question the credibility of information provided by transferors about transferred financial assets given recent market events.

A61. This proposed Statement also would simplify the accounting for transfers of financial assets by removing a complex area of accounting—the concept of a qualifying SPE—and subjecting all SPEs to the same accounting literature.

A62. The following are some of the benefits of this proposed Statement:

a. It would provide expanded information to financial statement users about a transferor's continuing involvement in transferred financial assets.
b. It would improve comparability in financial reporting by eliminating the exception for qualifying SPEs from the consolidation guidance. As a result, it would require consistent principles of consolidation for all entities by requiring that a transferor evaluate all transferees, including variable interest entities, for consolidation under the same applicable accounting guidance.
c. It would improve consistency in the application of reported financial information by clarifying the requirements for isolation of a transferred financial asset in its entirety, a group of financial assets in their entirety, and a participating interest in an individual financial asset.
d. It would provide more relevant financial information that better captures the economic substance of many transfers. For example, it would require initial measurement to be at fair value for beneficial interests received by a transferor if the transfer has met 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 securitization of financial assets.
e. It would require a transferor to provide additional disclosures to help users of financial statements 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.

A63. The Board recognizes that some entities may incur significant costs to (a) restructure existing entities, (b) develop and implement changes to information systems, (c) implement new internal controls, (d) restructure existing transaction agreements to maintain an accounting result in accordance with the proposed revised guidance, and/or (e) 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 impact of changes due to this proposed Statement on those calculations and to make any adjustments that they deem necessary to capital adequacy calculations. It is not possible to estimate those costs, in part because they are elective and some entities may choose not to restructure existing arrangements. 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 proposed amendments to Statement 140 are necessary to provide relevant, understandable, and transparent financial information to the capital markets.

Appendix B

AMENDMENTS TO EXISTING PRONOUNCEMENTS

B1. This Statement supersedes FASB Staff Position FAS 140-2, *Clarification of the Application of Paragraphs 40(b) and 40(c) of FASB Statement No. 140*.

B2. 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~~,~~ securitization that meets the requirements for a sale under paragraph 9 of Statement 140, as amended by FASB Statement No. 16X, *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 by the transferor 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 a sale under paragraph 9 of Statement 140, as amended by Statement 16X.

B3. 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.~~

B4. 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 of the following situations:
>
> a. A transfer of a servicer's individual financial asset in its entirety, a group of the servicer's financial assets in their entirety, or a participating interest in a servicer's individual ~~the servicer's~~ financial asset~~s~~ that meets the requirements for sale accounting
>
> ~~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 in which the transferor retains all of 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 asset 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.~~

B5. FASB Statement No. 157, *Fair Value Measurements*, is amended as follows:

a. Footnote 2 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, *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."

B6. 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).~~

B7. 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 of the following situations:

a. A transfer of <u>a servicer's individual financial asset in its entirety, a group of the servicer's financial assets in their entirety, or a participating interest in a servicer's individual</u> ~~the servicer's~~ financial asset~~s~~ that meets the requirements for sale accounting

~~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 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.~~

B8. Statement 133 Implementation Issue No. D1, "Recognition and Measurement of Derivatives: 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 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, 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.~~

B9. Statement 133 Implementation Issue No. F8, "Fair Value Hedges: Hedging Mortgage Servicing Right Assets Using Preset Hedge Coverage Ratios," is amended as follows:

[For ease of use, only the portions of this Implementation Issue affected by this Statement have been reproduced.]

BACKGROUND

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 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 transfer of a servicer's individual financial asset in its entirety, a group of the servicer's financial assets in their entirety, or a participating interest in a servicer's individual ~~the servicer's~~ financial asset~~s~~ that meets the requirements for sale accounting

~~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 SPE in a guaranteed mortgage securitization in which the transferor retains all of 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, which contains amendments to other authoritative literature, was issued separately on September 19, 2008 as "Amendments to Other Authoritative Literature." Due to the length of the appendix, it will be available as a separate document on the FASB website and will not be included directly in this document.]

Appendix D

STATEMENT 140 MARKED TO SHOW CHANGES THAT WOULD BE MADE BY THIS STATEMENT

D1. This Statement would amend 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 integrate changes from the Statement: 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.

D2. If the Statement was adopted as exposed, Statement 140 would read as follows: [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 are **recourse,** servicing, agreements to reacquire, options written or held, and pledges of **collateral.** 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.

[1]Terms defined in Appendix E, the glossary, are set in **boldface type** the first time they appear.

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. 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~~ interest that continues to be held by a transferor becomes an asset separate from the ~~portion~~ interest 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

[2]Contributions—unconditional nonreciprocal transfers of assets—are addressed in FASB Statement No. 116, *Accounting for Contributions Received and Contributions Made.*

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 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 Statement 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 issued Statement 125 in June 1996. The Board received a number of requests subsequent to the issuance of Statement 125 to reconsider or clarify the conditions for sale accounting and to expand the disclosure requirements in Statement 125. In response to those requests, the Board decided to amend Statement 125 and to replace it with Statement 140, even though most of the provisions of Statement 125 were carried forward to Statement 140 without reconsideration. The Board continued to receive requests from preparers and auditors to address various application issues. The Board decided to undertake a project to amend Statement 140 to address those concerns. During that project, in response to significant events in the credit markets, financial statement users requested limitations on sale accounting and additional disclosures. The Board concluded that a number of changes to the derecognition model were necessary to identify situations in which a transferor continues to maintain control of the transferred financial assets to such an extent that derecognition of the financial assets was not appropriate. The Board decided to amend Statement 140 with Statement 16X in 2008 to strengthen the guidance on control and to require additional disclosures.

~~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 guidance is to determine whether a transferor and all of the entities included in the financial statements being presented have surrendered control over transferred financial assets. This determination 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 individual financial asset in its entirety, transfers of groups of financial assets in their entirety, and transfers of a **participating interest** in an individual financial asset (which are referred to collectively in this Statement as *transferred financial assets*). A participating interest has the following characteristics:

a. It represents a proportionate ownership interest in an entire individual financial asset other than an equity instrument, a **derivative financial instrument,** or a hybrid financial instrument with an embedded derivative that is not clearly and closely related as described in Statement 133.

b. All cash flows received from the asset are divided among the participating interests (including any interest retained by the transferor, its **consolidated affiliates** included in the financial statements being presented, or its **agents**) in proportion to the share of ownership represented by each. Cash flows allocated to a servicer as compensation for servicing activities, if any, shall not be included in that determination. The transferor's ownership shares must remain pro rata over the life of the original financial asset. Participating interests may be further apportioned by the transferor as long as the resulting portions meet the definition of a participating interest.

c. The rights of each participating interest holder (including the transferor if it retains a participating interest) have the same priority, and that priority does not change in the event of bankruptcy or other receivership of the transferor, the original debtor, or any participating interest holder. Participating interest holders have no recourse, other than standard representations and warranties, to the transferor (or its consolidated affiliates included in the financial statements being presented or agents) or to each other, and no participating interest holder is subordinated to another. That is, no participating interest holder is entitled to receive cash before any other participating interest holder in its role as a participating interest holder.

d. No party has the right to pledge or exchange the entire financial asset.

If a transfer of a portion of an individual 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 an individual 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.

9. A transfer of an individual financial asset in its entirety, a group of financial assets in their entirety, or a participating interest in an individual 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 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 included in the financial statements being presented. For multiple step transfers, a special-purpose entity (SPE)[2a] that is designed to make remote the possibility that it would enter bankruptcy or other receivership (bankruptcy-remote entity) is not

[2a]For purposes of this Statement, the term *SPE* includes, but is not limited to, any entity whose activities are primarily related to securitization or other forms of asset-backed financings.

considered a consolidated affiliate for purposes of performing the isolation analysis[2b] (paragraphs 27, 28, and 83).

~~b. Each transferee (or, if the transferee is a qualifying SPE (paragraph 35), each 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 holder) from taking advantage of its right to pledge or exchange and provides more than a trivial benefit to the transferor (paragraphs 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. Judgment is required to assess whether a particular agreement provides the transferor with effective control of the transferred financial asset. For example, effective control over the transferred financial assets by the transferor exists 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) the ability to unilaterally cause the holder to return specific financial assets, other than through a **cleanup call** (paragraphs 50–54), (3) a restriction on the transferee's right to pledge or exchange the transferred financial asset it receives unless such constraint is designed primarily to provide the transferee with a benefit (paragraphs 54A–54D), or (4) 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 the transferred financial assets (paragraph 54E).

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).~~

[2b]Notwithstanding the isolation analysis, each SPE involved in the transfer is subject to the applicable guidance on whether it must be consolidated. For additional guidance on the isolation analysis, see paragraph 83.

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

a. Allocate the previous carrying amount between the participating interests sold and the participating interest that continues to be held by the transferor based on their relative fair values at the date of the transfer (paragraphs 58–60)
b. Derecognize the participating interest or interests sold
c. Recognize and initially measure at fair value assets obtained or liabilities incurred, including servicing assets or servicing liabilities, from the sale of the participating interest(s)
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 and the amount derecognized.

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

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 Financial Assets

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

a. Derecognize ~~all~~the transferred financial assets in their entirety~~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 (paragraphs 56–59 and 61–66), and any other assets obtained

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[2c]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, 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.

[3]See footnote 2c.~~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.~~

(including the transferor's **beneficial interest** or any other interests in the transferred financial assets) and liabilities incurred[3a] in the sale~~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 individual financial asset in its entirety or a group of financial assets in their entirety 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 individual financial asset~~s~~ in its entirety, a group of financial assets in their entirety, or a participating interest in an individual financial asset 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~~,~~ or if a transfer of a portion of an individual financial asset does not meet the definition of a participating interest, 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.

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 any of the following situations:

a. A transfer of a servicer's individual financial asset in its entirety, a group of the servicer's financial assets in their entirety, or a participating interest in a servicer's individual financial asset ~~the servicer's financial assets~~ that meets the requirements for sale accounting

~~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.

[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).

~~An entity that transfers its 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 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.~~

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 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, 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

[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.

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

<u>16A. The principal objectives of the disclosures required by paragraph 17 are to provide users of the financial statements with an understanding of:</u>

<u>a. A transferor's continuing involvement in financial assets that it has transferred to an SPE</u>
<u>b. The nature of any restrictions on assets reported by an entity in its statement of financial position, including the carrying amounts of such assets</u>
<u>c. How servicing assets and servicing liabilities are reported under this Statement</u>
<u>d. How a transfer of financial assets affects an entity's financial position, financial performance, and cash flows.</u>

<u>A reporting entity shall consider these overall objectives in providing the disclosures required by this Statement.</u>

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

[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.

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.

16C. To apply the disclosures in paragraph 17, all involvements by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents shall be considered involvement by the transferor.

17. In addition to the disclosures required by other standards, a~~A~~n entity shall disclose the following:

a. If assets are restricted solely to satisfy a specific obligation, the carrying amount of those assets and associated liabilities, including a description of the nature of restrictions placed on the assets.

~~a~~b. 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 amount and classification of those assets as of the date of the latest statement of financial position presented
  (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~~c. 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. For all servicing assets and servicing liabilities:
  (1) Management's basis for determining its classes of servicing assets and servicing liabilities (see paragraph 13A).

[6]~~Refer to footnote 11 to paragraph 19.~~

(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.

f. 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 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, 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(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. 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, assumption of servicing obligations, and 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, 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(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) 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) 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. If the entity has ~~securitized~~transferred financial assets to an SPE 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) 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.~~

(1~~2~~)The characteristics of the transfer ~~securitizations~~ (including a description of the transferor’s continuing involvement with the transferred financial assets, if any~~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 financial assets~~ in securitizations~~, including quantitative information about how the gain or loss was determined

(2~~3~~) The methodology, key inputs, and assumptions[7] used in measuring the fair value of assets obtained (including the transferor’s beneficial interests and any other interests in the transferred financial assets) and liabilities incurred in the sale~~interests that continue to be held by the transferor and servicing assets or servicing liabilities~~, if any, at the time of transfer~~securitization~~ (including, at a minimum, 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~~)

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

i. If the ~~entity has interests that continue to be held by the~~ transferor has continuing involvement in financial assets that it has ~~securitized~~transferred to an SPE (including those transfers that are accounted for as sales and those that are accounted for as secured borrowings) ~~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)~~:

(1) Qualitative and quantitative information about the transfer, giving consideration to both explicit and implicit arrangements, that provides users with sufficient information to assess 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:

(a) The transferor’s continuing involvement with the transferred financial assets

(b) The carrying amount and classification of assets and associated liabilities recognized in the transferor’s statement of financial position at the reporting date, including qualitative information about the relationship(s) between those assets and associated liabilities

(c) The terms of any arrangements that could require the transferor to

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[7]If an entity has aggregated ~~made~~ multiple ~~securitizations~~ transfers ~~of the same major asset type~~ during a period in accordance with paragraph 16B, 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.

provide financial support (for example, liquidity commitments 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

(d) 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:

(i) The type and amount of noncontractual support

(ii) The primary reasons for providing the noncontractual support.

(e) Liquidity, guarantees, and other commitments provided by third parties related to the transferred financial assets.

(2~~1~~) Its accounting policies for subsequently measuring ~~those interests~~assets or liabilities that relate to the continuing involvement in 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~~

(3~~2~~) The methodology, key inputs, and assumptions used in subsequently measuring the fair value of ~~those interests~~any assets or liabilities that relate to the transferor's continuing involvement (including, at a minimum, if applicable, quantitative information about discount rates, expected prepayments including the expected weighted-average life of prepayable financial assets, and anticipated credit losses, including expected static pool losses,[9] ~~if applicable~~)[9a]

(4~~3~~) A sensitivity analysis or stress test showing the hypothetical effect on the fair value of ~~those interests~~any assets or liabilities that relate to continuing involvement of the transferor (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 (~~2~~3) 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

(5) Cash flows during the period between a nonconsolidated SPE and the transferor (including proceeds from new transfers, proceeds from collections reinvested in revolving-period transfers, purchases of previously transferred financial assets [or its underlying collateral], servicing fees, and cash flows received on the transferor's interests)

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[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 financial assets.

[9a]The timing and amount of future cash flows for ~~retained~~ transferor's interests in ~~securitizations~~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~~securitized~~, because of the implicit credit or prepayment risk enhancement arising from the subordination.

(6~~4~~) For the transferred financial ~~securitized~~ assets and any other financial assets that it manages together with them:~~[10]~~

(a) The total principal amount outstanding, the amount ~~portion~~ that has been derecognized, and the amount ~~portion~~ that continues to be recognized in each category reported in the statement of financial position, at the end of the period

(b) Delinquencies at the end of the period

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

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

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 Statement 140 have passed. For the transition and effective date provisions of these amendments, see paragraphs 5–6 of this proposed Statement.]

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.

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 transferred financial assets have been isolated—put presumptively beyond the reach of the transferor, any of its consolidated affiliates (that are not SPEs 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

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

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 where 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), whether the transferor is affiliated with the transferee, and other factors pertinent under applicable law. Derecognition ~~of transferred assets~~ for transfers of an individual financial asset in its entirety, a group of financial assets in their entirety, or a participating interest in an individual financial asset (which are referred to collectively in this Statement as *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 SPEs designed to make remote the possibility that they would enter bankruptcy or other receivership) included in the financial statements being presented ~~**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, 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 with the assets and liabilities of the transferor or 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 it had no continuing involvement in the transferred financial assets or had experience with other transfers with the same facts and circumstances under similar applicable laws and regulations.

27B. 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.

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 (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 for surrender of control.

~~Conditions That Constrain a Transferee~~

~~29. Sale accounting is allowed under paragraph 9(b) only if each transferee 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. 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. 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.~~

~~30. However, some conditions do not constrain a transferee from pledging or exchanging the 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, because that right in itself does not enable the transferor to compel the transferee to sell the assets and the transferee would be in a position to receive the sum offered by exchanging the asset, albeit possibly from the transferor rather than the third party. Further examples of conditions that presumptively would not constrain a transferee 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 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~~

~~32. Some rights or obligations to reacquire transferred assets 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 **freestanding call** option written by a transferee to the transferor benefits the transferor and, if the transferred assets are not readily obtainable in the marketplace, is likely to constrain a transferee because it might have to default if the call was exercised and it had exchanged or pledged the assets. A freestanding forward purchase-sale contract between the transferor and the transferee on transferred 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 rights to reacquire transferred assets that are readily obtainable presumptively do not constrain the transferee from exchanging or pledging them and thus do not preclude sale accounting under paragraph 9(b).~~

~~33. Other rights or obligations to reacquire transferred assets, regardless of whether they constrain the transferee, may result in the transferor's maintaining effective control over the transferred assets, as discussed in paragraphs 50–54, thus precluding sale accounting under paragraph 9(c)(2).~~[15]

~~[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.~~

~~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.~~

~~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~~

~~[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.~~

~~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.~~

~~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~~

~~[17]An 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.~~

~~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

46A. To assess whether the transferor maintains effective control over the transferred financial assets, all involvements by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents shall be considered involvement by the transferor.

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 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 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

[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*.

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.

Ability to Unilaterally Cause the Return of Specific Transferred Financial Assets

50. Some rights to reacquire transferred financial assets (or to acquire beneficial interests in transferred financial 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 financial assets through the **unilateral ability** to cause the return of specific transferred financial assets~~. Such rights preclude sale accounting~~ as described in ~~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~~ a transferred financial asset~~(s)~~ because the attached call gives the transferor the ability to unilaterally cause whoever holds that specific financial asset to return it. In contrast, a transfer~~s~~ of a financial asset~~s~~ subject to a call~~s~~ embedded by the issuers of the financial instruments, for example, callable bonds or prepayable mortgage loans, does 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.

~~51. If the transferee is a qualifying SPE, it has met the conditions in paragraph 35(d) and therefore must be constrained from choosing to exchange or pledge the transferred assets. In that circumstance, any call held by the transferor is effectively attached to the assets and could—depending on the price and other terms of the call—maintain the transferor’s effective control over transferred 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 a transferred financial asset~~s~~ may provide~~maintains~~ the transferor~~'s~~ with effective control over ~~those~~ that financial asset~~s~~ based on the~~if, under its~~ price and other terms~~,~~ of 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 provides the transferor with effective control~~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 a specific transferred financial asset~~s transferred to a qualifying SPE~~ at a price fixed at ~~their~~ its principal amount maintains the transferor's effective control over the financial asset~~s~~ subject to that call. Effective control over transferred financial 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 an ~~qualifying~~ SPE at a fixed price, then the transferor remains in effective control of the financial assets underlying those beneficial interests. Additionally, depending on the price and other terms of the call, a call that provides the transferor with the unilateral ability to cause an SPE to return to the transferor or otherwise dispose of specific transferred financial assets at will, for example, in response to the transferor's decision to exit a market or a particular activity, could provide the transferor with effective control over the transferred financial assets. A cleanup call, however, is permitted as an exception to that general principle.

53. A right to reclaim specific transferred financial assets by paying their fair value when reclaimed generally does not maintain effective control~~, because it does not convey a more than trivial benefit to the transferor~~. However, a transferor may ~~has~~ maintain~~ed~~ effective control if it has such a right and also holds a ~~the~~ residual interest in the transferred financial assets. For example, if a transferor holds a residual interest in securitized financial assets and can reclaim ~~such~~the transferred financial assets at termination of the securitization~~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.

53A. The transferor must evaluate whether the combination of multiple arrangements maintains effective control of transferred financial assets. For example, if the transferor as the servicer for the transferred financial asset is empowered to offer the financial asset for sale and has the right of first refusal to purchase the financial asset, that combination of circumstances would place the transferor in a position to unilaterally cause the return of a specific transferred financial asset and thus maintain the transferor's effective control of the transferred financial asset.

54. A transferor that has a right to reacquire transferred financial assets from a transferee~~qualifying SPE~~ does not maintain effective control if the reclaimed financial assets would be randomly selected and the amount of the financial assets reacquired is sufficiently limited (paragraph 87(a)), because that would not be a right to reacquire *specific* financial assets. Nor does a transferor maintain effective control through an obligation to reacquire transferred financial assets ~~from a 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 transferee~~qualifying SPE~~ to repurchase that beneficial interest ~~(paragraph 44(b))~~, because the transferor could not cause that reacquisition *unilaterally*. Similarly, freestanding rights to reacquire transferred financial assets that are readily obtainable presumptively do not cause a transferor to maintain effective control. On the other hand, a **freestanding call** option written by a transferee to the transferor benefits the transferor and, if the transferred financial assets are not readily obtainable in the marketplace, is likely to cause a transferor to maintain effective control because the transferee might have to default if the call was exercised and the transferee had exchanged or pledged the financial assets. In much the same manner, 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 result in the transferor maintaining effective control as the transferee is constrained.

Conditions That Constrain a Transferee

54A. A transferor maintains effective control over a transferred financial asset as described in paragraph 9(c)(3) if the transferee is constrained from pledging or exchanging the transferred financial asset it received and the constraint is not designed primarily to provide the transferee with a benefit. However, a transferor does not maintain effective control over a transferred financial asset if a constraint on the transferee's right to pledge or exchange the transferred financial asset is designed primarily to provide the transferee with a benefit. For example, in many securitization transactions, the transferee is restricted from pledging or exchanging the transferred financial asset. However, such restriction may exist primarily to benefit the transferee because it enhances the transferee's ability to market the issuance of securities backed by the transferred financial assets to prospective beneficial interest holders. Accordingly, the transferor does not maintain effective control over the transferred financial asset solely due to that constraint.

54B. Alternatively, a constraint on the transferee's right to pledge or exchange the transferred financial asset that is not designed primarily to provide the transferee with a benefit would provide the transferor with effective control over the transferred financial asset. For example, a provision that prohibits the transferee from selling or pledging a transferred loan receivable, which provides the transferor with the knowledge of who has the financial asset (a prerequisite to repurchasing the financial asset) and may block the financial asset from finding its way into the hands of a competitor, provides no benefit to the transferee. The transferee's ability to receive the economic benefits of the transferred financial asset (that is, to collect cash flows from the transferred financial asset) does not result in the transferee receiving a benefit from the constraint.

54C. Some conditions do not constrain a transferee from pledging or exchanging the financial asset and, therefore, do not provide the transferor with effective control over the transferred financial asset. 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 the right in itself does not enable the transferor to compel the transferee to sell the 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.

54D. Judgment is required to assess whether a particular condition results in a constraint and, if so, whether that constraint is designed primarily to provide a benefit to the transferee. Judgment also is required in assessing the significance of the benefit and whether the constraint provides the transferor with the ability to effectively control the transferred financial asset. It is necessary to consider the overall effect of related rights and obligations in assessing such matters as whether (a) a transferee is constrained, (b) the transferee receives a benefit from such constraint, and (c) the transferor maintains effective control over the transferred financial assets. For example, a prohibition on sale to the transferor's competitor would be a constraint if that competitor was the only potential willing buyer other than the transferor.

Arrangements to Reacquire Transferred Financial Assets

54E. A transferor maintains effective control over the transferred financial asset as described in paragraph 9(c)(4) 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 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 the transferor's regaining control of transferred financial assets subsequent to 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 a change, unless it arises solely from (a) ~~either~~ the initial application of this Statement, (b) consolidation of an entity involved in the transfer at a subsequent date (see paragraph 55A), or (c) 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), 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 paragraph 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 of the former transferee(s)~~in those assets (paragraph 38)~~. 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~~ loans in their entirety to an SPE with a fair value of $1,100 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~~
Carrying amount of loans sold	1,000
Gain on sale	$30~~$ 100~~

[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.

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		

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 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 asset has a fair value of zero ~~There is no servicing asset or liability,~~ because Company B estimates that the **benefits of servicing**

[18b]See footnote 18a.

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 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 transferor	110	10	100
Total	$1,100	100	$1,000

Gain on Sale

Net proceeds	$990
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 a financial asset, it would recognize a servicing asset or servicing liability that qualifies for

recognition, if any, related to the participating interest sold, but would not recognize a separate servicing asset or servicing liability related to the participating interest that it continues to hold.

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 transfer of a servicer’s individual financial asset in its entirety, a group of the servicer’s financial assets in their entirety, or a participating interest in a servicer’s individual 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 (b~~c~~) 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 in a guaranteed mortgage securitization, retains all of 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.
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,

[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.

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 $1,050, gain on sale would be reduced to $50, 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 transfers ~~sells~~ the loans in their entirety 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~~ 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.

[19a]See footnote 18a.

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.~~

~~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.]

20–21[These footnotes 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.~~

~~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 an SPE, commonly a trust. In "pass-through" and "pay-through" securitizations, receivables are transferred to the SPE 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 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 uses most of the cash collections to purchase additional receivables from the transferor on prearranged terms.

75. Beneficial interests in the 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 SPE.

76. Pass-through, pay-through, and revolving-period securitizations that meet the criteria in paragraph 9 qualify for sale accounting under this Statement. 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. To achieve sale accounting for ~~R~~revolving-period securitizations, a transferor 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 SPEs 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 paragraph 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, if it failed, transfers financial assets to an SPE~~special-purpose trust~~ in exchange for cash. The SPE~~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 SPEs 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 an SPE in exchange for cash and beneficial interests in the transferred financial asset~~s~~. That SPE~~entity~~ raises the cash by issuing to investors commercial paper that gives them a senior beneficial interest in cash received from the financial asset~~s~~. The beneficial interests received ~~that continue to be held~~ by the transferring corporation represent a junior interest to be reduced by any credit losses on the financial asset~~s~~ in the SPE~~trust~~. The senior beneficial~~commercial paper~~ interests (the 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 asset~~s~~, 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 asset~~s~~ beyond the reach of the transferor, its consolidated affiliates (that are not SPEs 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 asset~~s~~ 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 SPEs 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 financial assets to a consolidated SPE ~~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 SPEs 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 SPE~~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 SPEs 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 SPE~~special-purpose corporation~~ transfers ~~the~~ an individual financial asset~~s~~ in its entirety, a group of financial assets in their entirety, or a participating interest in an individual financial asset to a trust or other legal vehicle with a sufficient increase in the credit or yield protection on the second transfer (provided by a junior beneficial transferor interest's ~~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 SPE~~special-purpose corporation~~.

c. However, the SPE~~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 SPEs 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 SPE involved in a transfer must be evaluated under the applicable consolidation 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 Federal Deposit Insurance Corporation (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 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 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 (paragraphs 9(c)(2) and ~~51~~50–54).

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, 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, 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, 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 are recognized because the transferor now can unilaterally cause the transferee~~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 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.[21b] 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. 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

[21b] 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, the criteria 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 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.

[22]If the "collateral" in a transaction that meets the criteria 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.

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.

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 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

[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).

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 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]~~transferee 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 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 unless the

constraint is designed primarily to provide the transferee with a benefit.

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 an~~undivided~~ interest~~s~~ 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 a 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 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 transferees from pledging or exchanging their ~~participations~~participating interest~~, the transferor presumptively receives a more than trivial benefit~~, the transferor generally has not relinquished control over the participating interest unless the constraint meets the criteria in paragraph 9(c)(3)~~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:

<u>Facts</u>

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

<u>Journal Entries for Accepting Bank</u>

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 are sold in their entirety 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 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 a receivable~~s~~ in its entirety, a group of receivables in their entirety, or a participating interest in an individual receivable with recourse, the transferor provides the transferee with full or limited recourse. A transfer of a portion of a receivable that does not meet the requirements of a participating interest 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 SPEs 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 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 in paragraph 9 are met. Otherwise, a transfer of receivables with recourse shall be accounted for as a secured borrowing.

Transfers of a Senior Interest in Receivables

113A. In other cases, a transferor may transfer a portion of an individual receivable or a group of receivables that represent a senior interest in an individual receivable or a group of receivables. In those cases, the transferor would account for the transfer as a secured borrowing because the senior interest in the receivable or group of receivables does not meet the requirements to be a participating interest.

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 key assumptions used in measuring interests that continue to be held by the transferor at the date of sale or securitization for each financial period presented (paragraph17(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~~	~~Fixed-Rate~~	~~Adjustable~~[†]
~~Prepayment speed~~	~~1.00%~~	~~15.0%~~	~~10.00%~~	~~8.0%~~	~~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.~~

~~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):~~

~~[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.~~

	~~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.~~

[34]~~Footnote 8, paragraph 17(h)(3), describes how weighted-average life can be calculated.~~

~~347. The following is an illustration of disclosure of expected static pool credit losses (paragraph 17(i)(2)).~~

	~~Automobile Loans Securitized in~~		
~~Actual and Projected Credit Losses (%) as of:~~	**~~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.~~

~~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):~~

~~Type of Loan~~	~~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~~			
	~~20X2~~	~~20X1~~	~~20X2~~	~~20X1~~	~~20X2~~	~~20X1~~	~~20X2~~	~~20X1~~
~~Automobile loans~~	~~$830~~	~~$488~~	~~$42.3~~	~~$26.8~~	~~$720~~	~~$370~~	~~$21.6~~	~~$12.6~~
~~Residential mortgage loans (fixed-rate)~~	~~482~~	~~302~~	~~5.8~~	~~3.6~~	~~470~~	~~270~~	~~5.6~~	~~3.2~~
~~Residential 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.~~

~~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)):~~

[35]~~This disclosure is optional.~~

[36]~~Loans held in portfolio are reported separately from loans held for securitization because they are measured differently.~~

~~Tabular Disclosure 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 the 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 Disclosure 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 received by an SPE~~to 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 (or in a series of beneficial interests in transferred financial assets within an ~~qualifying~~ SPE), 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. Examples of continuing involvement include, but are not limited to, servicing arrangements, recourse or guarantee arrangements, agreements to purchase or redeem transferred financial assets, derivative instruments related to the transferred financial assets, implicit commitments to provide financial support, pledges of collateral, or the transferor's beneficial interests.

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. It represents a proportionate ownership interest in an entire individual financial asset other than an equity instrument, a derivative financial instrument, or a hybrid financial instrument with an embedded derivative that is not clearly and closely related as described in Statement 133.
b. All cash flows received from the asset are divided among the participating interests (including any interest retained by the transferor, its consolidated affiliates included in the financial statements being presented, or its agents) in proportion to the share of ownership represented by each. Cash flows allocated to a servicer as compensation for servicing activities, if any, shall not be included in that determination. The transferor's ownership shares must remain pro rata over the life of the original financial asset. Participating interests may be further apportioned by the transferor as long as the resulting portions meet the definition of a participating interest.
c. The rights of each participating interest holder (including the transferor if it retains a participating interest) have the same priority, and that priority does not change in the event of bankruptcy or other receivership of the transferor, the original debtor, or any participating interest holder. Participating interest holders have no recourse, other than standard representations and warranties, to the transferor (or its consolidated affiliates included in the financial statements being presented or agents) or to each other, and no participating interest holder is subordinated to another. That is, no participating interest holder is entitled to receive cash before any other participating interest holder in its role as a participating interest holder.
d. No party has the right 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.

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 an individual financial asset in its entirety, ~~a portion of a financial asset, or~~ a group of financial assets in their entirety, or a participating interest in an individual financial asset from a transferor.

Transferor

An entity that transfers an individual financial asset in its entirety, ~~a portion of a financial asset, or~~ a group of financial assets in their entirety, or a participating interest in an individual financial asset 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.