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Financial Accounting Series

EXPOSURE DRAFT

Proposed Statement of Financial Accounting Standards

The Fair Value Option for Financial Assets and Financial Liabilities

Including an amendment of FASB Statement No. 115

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. 1250-001

Comment Deadline: April 10, 2006

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 April 10, 2006. Interested parties should submit their comments by email to director@fasb.org, File Reference 1250-001. Those without email may send their comments to the "Technical Director—File Reference 1250-001" 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.

Any individual or organization may obtain one copy of this Exposure Draft without charge until April 10, 2006, on written request only. *Please ask for our Product Code No. E188.* For information on applicable prices for additional copies and copies requested after April 10, 2006, contact:

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Notice for Recipients
of This Exposure Draft

The fair value option project has two phases: This proposed Statement represents Phase 1, which addresses the fair value option for certain financial assets and financial liabilities. Phase 2 will consider permitting the fair value option for certain nonfinancial assets and nonfinancial liabilities and some of the financial assets and financial liabilities excluded from the scope of Phase 1.

This proposed Statement would create a fair value option under which an entity may irrevocably elect fair value as the initial and subsequent measurement attribute for certain financial assets and financial liabilities on a contract-by-contract basis, with changes in fair value recognized in earnings as those changes occur. The Board invites comments on all matters in this proposed Statement, particularly on the specific issues discussed below. Respondents need not comment on all of those issues and are encouraged to comment on additional issues. 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 specific paragraph or group of paragraphs to which they relate and clearly explain the problem or question. Those who disagree with the provisions of this proposed Statement are asked to describe their suggested alternatives, supported by specific reasoning.

Scope

Issue 1: The scope of this proposed Statement includes the following financial assets and financial liabilities that some may not have considered as being included:

a. An investment being accounted for under the equity method
b. Investments in equity securities that do not have readily determinable fair values, as described in paragraph 3 of FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*
c. Insurance and reinsurance contracts that are financial instruments, as discussed in FASB Statements No. 60, *Accounting and Reporting by Insurance Enterprises*, No. 97, *Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments,* and No. 113, *Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts*
d. Warranty obligations that are financial liabilities and warranty rights that are financial assets
e. Unconditional purchase obligations that are recorded as financial liabilities on the purchaser's statement of financial position as discussed in paragraph 10 of FASB Statement No. 47, *Disclosure of Long-Term Obligations*.

Should an entity not be permitted the option to initially and subsequently measure those financial assets and financial liabilities or any others at fair value? If so, why should those financial assets and financial liabilities be excluded from the scope of this proposed Statement?

Issue 2: This proposed Statement permits an entity to elect the fair value option at inception for a firm commitment that would otherwise not be recognized at inception under existing generally accepted accounting principles (GAAP) and involves only financial instruments. Should an entity be permitted the option to recognize those firm commitments at fair value at inception of the contract? If so, why is the availability of the fair value option election important for those contracts and what types of entities would likely avail themselves of that fair value option election? Should the scope be limited to forward contracts that meet the definition of *firm commitments* under FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities* (that is, requiring that the terms of the forward contract include a disincentive for nonperformance that is sufficiently large to make performance probable)? If not, why not?

Issue 3: The scope of this proposed Statement would exclude both (a) written loan commitments that are not accounted for as derivative instruments under Statement 133 and (b) financial liabilities for demand deposit accounts. The Board decided to specifically exclude those financial instruments, since the determination of their fair values involves consideration of nonfinancial components. Should an entity be permitted the fair value option election for those financial instruments? If so, why? What would be the appropriate unit of account for determining the fair value of demand deposit liabilities? What other financial assets and financial liabilities for which their fair values involve consideration of nonfinancial components should be excluded from the scope of this proposed Statement?

Issue 4: The scope of this proposed Statement would also exclude:

a. An investment that would otherwise be consolidated
b. Employers' and plans' financial obligations for pension benefits, other postretirement benefits (including health care and life insurance benefits), postemployment benefits, employee stock option and stock purchase plans, and other forms of deferred compensation arrangements as defined in FASB Statements No. 35, *Accounting and Reporting by Defined Benefit Pension Plans,* No. 87, *Employers' Accounting for Pensions*, No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions*, No. 112, *Employers' Accounting for Postemployment Benefits,* No. 123 (revised December 2004), *Share-Based Payment,* No. 43, *Accounting for Compensated Absences,* and No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*, and APB Opinion No. 12, *Omnibus Opinion—1967*
c. Financial liabilities recognized under lease contracts as defined in FASB Statement No. 13, *Accounting for Leases.* (This exclusion does not include a contingent obligation arising out of a cancelled lease or a guarantee of a third-party lease obligation.)

The Board decided to specifically exclude those financial assets and financial liabilities from the scope of this proposed Statement, as the Board believes that any modifications to the accounting for such financial assets and financial liabilities should be part of a reconsideration of those areas and should not be affected by the fair value option. Should an entity be permitted the fair value option election for those financial instruments? If so, why?

Issue 5: As noted above, this proposed Statement represents Phase 1 of the fair value option project. Phase 2 will consider permitting the fair value option for selected nonfinancial assets and liabilities. The Board is seeking input on what nonfinancial instruments should be included in the scope of Phase 2. Please provide details of those nonfinancial instruments and why they should be eligible for the fair value option. How would applying the fair value option to those nonfinancial instruments (a) improve financial reporting, (b) mitigate problems for reported earnings caused by the mixed-attribute model, and (c) enable an entity to simplify its accounting methods? Is fair value information readily available for those nonfinancial instruments?

Changes in Creditworthiness

Issue 6: This proposed Statement would permit an entity to elect the fair value option for certain financial liabilities, including debt liabilities. Under this proposed Statement, an issuer who has elected the fair value option for its debt liabilities would report changes in fair value of those liabilities, including changes resulting from changes in that issuer's own creditworthiness, as gains and losses in earnings. If significant changes in fair value of those liabilities occur during a period, qualitative disclosures about the nature of those changes would be required. The Board discussed several possible approaches for curtailing the debtor's recognition of the portion of a liability's changes in fair value that is attributable to changes in its own creditworthiness and determined not to provide any curtailment; instead, the Board decided that liabilities should be recorded at fair value when the fair value option has been elected with all changes in fair value recorded in earnings. Do you agree with the Board's decision? If not, why not? What alternative approaches or additional disclosure requirements should the Board consider?

Presentation and Disclosure Requirements

Issue 7: The Board discussed several possible approaches for separately reporting changes in the fair values of financial assets and financial liabilities measured at fair value pursuant to the election of the fair value option in the income statement or in the notes to the financial statements. The Board decided that an entity should provide information that would allow users to understand the effect of changes in the fair values of assets and liabilities subsequently measured at fair value as a result of a fair value election, but it did not prescribe detailed guidance on where and how that information should be reported. How should changes in the fair values of assets and liabilities subsequently measured at fair value as a result of a fair value election be reported? Should those changes be aggregated with the effect on earnings derived from other similar financial assets and financial liabilities in the income statement, or should separate display of those changes in the income statement be required? What level of aggregation should be permitted? What additional disclosure requirements should the Board consider?

Summary

This proposed Statement would create a fair value option under which an entity may irrevocably elect fair value as the initial and subsequent measurement attribute for certain financial assets and financial liabilities, with changes in fair value recognized in earnings as those changes occur. An entity would be permitted to elect the fair value option at initial recognition of a financial asset or financial liability or upon an event that gives rise to new-basis accounting for that item. The election of the fair value option would be made on a contract-by-contract basis and would need to be supported by concurrent documentation or a preexisting documented policy.

This proposed Statement would require an entity to report its financial assets and financial liabilities that, pursuant to electing the fair value option, would be subsequently measured at fair value in a manner that separates those reported fair values from the carrying amounts of assets and liabilities subsequently measured using another measurement attribute on the face of the statement of financial position. To accomplish that separate reporting, an entity would either (a) display separate line items for the fair value and non-fair-value carrying amounts or (b) present the aggregate of those fair value and non-fair-value amounts and disclose parenthetically the amount of fair value included in the aggregate amount. This proposed Statement would amend FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, to require that securities reported at fair value in accordance with Statement 115 satisfy this financial statement presentation requirement.

This proposed Statement would also require an entity to provide information that would allow users to understand the effect on earnings of changes in the fair values of assets and liabilities subsequently measured at fair value as a result of a fair value election.

Reasons for Issuing This Proposed Statement and How It Would Improve Financial Reporting

Current GAAP requires some assets or liabilities to be reported using the fair value measurement attribute, while other related assets or liabilities are required to be reported using another measurement attribute. This mixed-attribute accounting leads to volatility in reported earnings. Creation of the fair value option would permit an entity to mitigate that volatility by enabling entities to achieve an offset accounting effect for the changes in the fair values of related assets and liabilities without having to apply complex hedge accounting provisions. Furthermore, issuance of this proposed Statement would achieve further convergence with the International Accounting Standards Board, which has incorporated a fair value option for financial instruments in its IAS 39, *Financial Instruments: Recognition and Measurement*.

How the Conclusions in This Proposed Statement Relate to the Conceptual Framework

FASB Concepts Statement No. 1, *Objectives of Financial Reporting by Business Enterprises*, states that financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit, and similar decisions. The Board believes that fair values for financial assets and financial liabilities provide more relevant and understandable information than cost or cost-based measures. In particular, the Board believes that fair value is more relevant to financial statement users than cost for assessing the current financial position of an entity because fair value reflects the current cash equivalent of the entity's financial instruments rather than the price of a past transaction.

The Board acknowledges that comparability between entities may be impaired to the extent that different entities with similar financial assets and financial liabilities apply different measurement attributes to those assets and liabilities. In addition, because the fair value option would be applied on a contract-by-contract basis within an entity, the provisions of this proposed Statement may result in different measurement attributes for similar financial assets and financial liabilities within an entity. The Board agrees that the provisions of this proposed Statement may impair comparability and consistency across entities, but it supports the provisions of this proposed Statement to enable greater use of fair value and convergence as well as achieve more representative, internally consistent financial reporting for entities that elect the fair value option to mitigate the effects of the mixed-attribute model.

Effective Date and Transition

Adoption of this proposed Statement would be required as of the beginning of an entity's first fiscal year that begins after December 15, 2006, with earlier adoption permitted as of the beginning of an entity's earlier fiscal year that begins after issuance of the final Statement.

As of the date of initial adoption, an entity would be permitted to elect the fair value option for any existing financial asset or financial liability within the scope of this proposed Statement. The adjustment to reflect the difference between the fair value and the carrying amount of the existing financial assets and financial liabilities for which an entity irrevocably elected the fair value option as of the date of initial adoption would be accounted for as a cumulative-effect adjustment to retained earnings. Retrospective application of the accounting provisions in this proposed Statement would not be permitted.

Proposed Statement of Financial Accounting Standards

The Fair Value Option for Financial Assets and Financial Liabilities

Including an amendment of FASB Statement No. 115

January 25, 2006

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Proposed Statement of Financial Accounting Standards

The Fair Value Option for Financial Assets and Financial Liabilities

Including an amendment of FASB Statement No. 115

January 25, 2006

OBJECTIVE

1. This Statement creates an alternative measurement treatment for certain financial assets and financial liabilities that permits fair value to be used for both initial and subsequent measurement, with changes in fair value recognized in earnings as those changes occur, based on a contract-by-contract election. The availability of that election is referred to as the fair value option. The Statement's objective is to improve financial reporting by providing entities a mechanism by which they can (a) mitigate volatility in reported earnings that is caused by an accounting model that uses multiple measurement attributes and (b) achieve an offset accounting effect for the changes in the fair values of related financial assets and financial liabilities without having to apply complex hedge accounting provisions. Establishing the option to elect fair value also achieves further convergence with the International Accounting Standards Board (IASB), which has incorporated a fair value option for financial instruments into its authoritative literature. It also expands the use of the fair value measurement attribute for financial instruments, which is considered to be more relevant to financial statement users than cost for assessing the current financial position of an entity.

2. Consistent with the objective to improve financial reporting, this Statement requires certain financial statement presentations and disclosures to compensate for the lack of comparability that will arise from the alternative measurement treatment permitted by this Statement. Those presentations and disclosures should assist users of financial statements in assessing the effects on an entity's financial position and results of operations from reporting selected financial assets and financial liabilities at fair value.

STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

Scope and Related Scope Exceptions

3. This Statement provides all entities with an alternative measurement treatment for recognized financial assets and financial liabilities, except as indicated in paragraph 4. It also establishes an alternative measurement treatment for certain unrecognized firm commitments. It does not apply to nonfinancial assets and nonfinancial liabilities.

4. The scope of this Statement excludes the following; as a result, the fair value option may not be elected for any of them:

a. An investment (principally an investment in a subsidiary) that would otherwise be consolidated.
b. Employers' and plans' financial obligations for pension benefits, other postretirement benefits (including health care and life insurance benefits), postemployment benefits, employee stock option and stock purchase plans, and other forms of deferred compensation arrangements as defined in FASB Statements No. 35, *Accounting and Reporting by Defined Benefit Pension Plans,* No. 87, *Employers' Accounting for Pensions,* No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions,* No. 112, *Employers' Accounting for Postemployment Benefits,* No. 123 (revised December 2004), *Share-Based Payment,* No. 43, *Accounting for Compensated Absences,* and No. 146, *Accounting for Costs Associated with Exit or Disposal Activities,* and APB Opinion No. 12, *Omnibus Opinion—1967.*
c. Financial liabilities recognized under lease contracts as defined in FASB Statement No. 13, *Accounting for Leases.* (This exclusion does not include a contingent obligation arising out of a cancelled lease or a guarantee of a third-party lease obligation.)
d. Written loan commitments that are not accounted for as derivative instruments under FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities.*
e. Financial liabilities for demand deposit accounts.

Key Terms

5. The following key terms are defined as used in this Statement:

a. **Financial asset—**Cash, evidence of an ownership interest in an entity, or a contract that conveys to a second entity a contractual right (a) to receive cash or another financial instrument from a first entity or (b) to exchange other financial instruments on potentially favorable terms with the first entity.
b. **Financial liability—**A contract that imposes on one entity a contractual 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.
c. **Firm commitment—**An agreement with an unrelated party, binding on both parties and usually legally enforceable, with the following characteristics:
    (1) The agreement specifies all significant terms, including the quantity to be exchanged, the fixed price, and the timing of the transaction. The fixed price may be expressed as a specified amount of an entity's functional currency or of a foreign currency. It may also be expressed as a specified interest rate or specified effective yield.
    (2) The agreement includes a disincentive for nonperformance that is sufficiently large to make performance probable.

Initial and Subsequent Measurement

6. On the date that a financial asset or financial liability is initially recognized or upon an event that gives rise to new-basis accounting at fair value under generally accepted accounting principles (GAAP), an entity may elect to use fair value as the initial and subsequent measurement attribute in accounting for that financial asset or financial liability. (For purposes of this Statement, a remeasurement ("new-basis") event is an event identified in other authoritative literature, other than the recognition of an other-than-temporary impairment, that requires a financial instrument to be remeasured to its fair value at the time of the event but does not require that instrument to be reported at fair value on a continuous basis with the change in fair value reported in the income statement. Examples of remeasurement events are business combinations and significant modifications of debt, as defined in EITF Issue No. 96-19, "Debtor's Accounting for a Modification or Exchange of Debt Instruments.") The election of the fair value option (a) is made on a contract-by-contract basis, (b) is irrevocable, and (c) requires that changes in fair value be recognized in earnings (or other performance indicators for entities that do not report earnings) as those changes occur. The election of the fair value option shall be supported by concurrent documentation or a preexisting documented policy for automatic election.

7. The election of the fair value option is also permitted at inception for a firm commitment that would otherwise not be recognized at inception under existing GAAP and that involves only financial instruments, such as a forward contract for the cash purchase of a nonmortgage loan that is not readily convertible to cash.

8. This Statement permits the election of the fair value option to be made on a contract-by-contract basis. However, an entity may not separate the cash flows under an individual contract and elect the fair value option for some cash flows but account for other cash flows under a different subsequent measurement attribute. Thus, for example, an insurance company may not elect the fair value option for the financial liabilities for only certain claims without also electing it for the financial liabilities for other claims under the same contract.

9. Business combinations accounted for under FASB Statement No. 141, *Business Combinations*, involve the acquisition of assets and the assumption or incurrence of liabilities. The acquiring entity's decision whether to elect the fair value option for specific assets acquired and liabilities assumed or incurred is not affected by any previous election of the fair value option by the entity that was acquired in the business combination. If a subsidiary is newly consolidated, the consolidation represents the initial recognition of those assets and liabilities by the consolidated reporting entity. Upon consolidation (or reconsolidation) of a subsidiary or a variable interest entity (as discussed in FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities*), the fair value option election is permitted for such newly consolidated assets and liabilities for purposes of reporting by the consolidated entity.

Financial Statement Presentation

Presentation on the Statement of Financial Position

10. An entity shall report its assets and liabilities that are subsequently measured at fair value pursuant to the election of the fair value option under this Statement in a manner that separates those reported fair values from the carrying amounts of assets and liabilities subsequently measured using another measurement attribute on the face of the statement of financial position. To accomplish that separate reporting, an entity may either (a) display separate line items for the fair value and non-fair-value carrying amounts or (b) present the aggregate of those fair value and non-fair-value amounts and parenthetically disclose the amount of fair value included in the aggregate amount.

Cash Flow Reporting

11. Cash receipts and cash payments related to financial assets and financial liabilities for which the fair value option has been elected shall be classified pursuant to FASB Statement No. 95, *Statement of Cash Flows* (as amended), based on the nature and purpose for which the related financial assets and financial liabilities were acquired or incurred.

Disclosure Requirements

12. An entity shall disclose the following with respect to financial assets and financial liabilities for which the fair value option has been elected:

a. The difference between the carrying amount of any financial liabilities reported at fair value due to election of the fair value option and the aggregate principal amount the entity would be contractually required to pay to the holders of the obligations at maturity (or through the maturity date for any debts whose principal amounts are payable in installments), if any
b. Information sufficient to allow users of financial statements to understand the effect on earnings (or other performance indicators for entities that do not report earnings) of changes in the fair values of the financial assets and financial liabilities subsequently measured at fair value as a result of a fair value election
c. Quantitative information by line item indicating where in the income statement gains and losses are reported that arise from changes in the fair value of financial assets and financial liabilities for which the fair value option has been elected
d. A description indicating how interest and dividends are measured and reported in the income statement.

The disclosures in subparagraph (a) are required as of each date for which a statement of financial position is presented. The disclosures in subparagraphs (b)–(d) are required for each period for which an income statement is presented. The above disclosure requirements do not eliminate disclosure requirements included in other GAAP pronouncements, including other disclosure requirements on the use of fair value measures.

13. With respect to financial liabilities for which the fair value option has been elected, if significant changes in the fair values of those liabilities occur in any period presented, an entity shall disclose qualitative information about the reasons for those changes.

Effective Date and Transition

14. This Statement shall be effective as of the beginning of each reporting entity's first fiscal year that begins after December 15, 2006, with earlier adoption permitted as of the beginning of an entity's earlier fiscal year that begins after issuance of this Statement. Upon adoption of this Statement as of the beginning of a fiscal year, the reporting entity may elect the fair value option for existing financial assets and financial liabilities that are within the scope of this Statement (including available-for-sale and held-to-maturity securities accounted for under FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*). The effect of the initial adoption of this Statement attributable to the election of the fair value option for the selected financial assets and financial liabilities existing at the effective date shall be accounted for as a cumulative-effect adjustment of retained earnings as of the effective date. Retrospective application of this Statement to fiscal years preceding the effective date is not permitted.

15. For available-for-sale and held-to-maturity securities previously accounted for under Statement 115 for which the fair value option has been elected upon the initial adoption of this Statement (thereby effectively reclassifying those securities as trading securities), the amount of the effect of that reclassification into the trading category (which is included in the cumulative effect adjustment of retained earnings) shall be separately disclosed. The effect of that reclassification that arose from the initial adoption of this Statement shall not be accounted for as a transfer between categories under paragraph 15(b) of Statement 115.

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

Appendix A

BACKGROUND INFORMATION, BASIS FOR CONCLUSIONS, AND ALTERNATIVE VIEWS

CONTENTS

Paragraph Numbers

Appendix A

BACKGROUND INFORMATION, BASIS FOR CONCLUSIONS, AND ALTERNATIVE VIEWS

Introduction

A1. This appendix summarizes considerations that Board members deemed significant in reaching the conclusions in this Statement. It includes reasons for accepting certain views and rejecting others. Individual Board members gave greater weight to some factors than to others.

Background Information

A2. In its projects on the accounting for servicing rights and hybrid financial instruments, the Board reached tentative decisions to permit entities to elect fair value as the subsequent measurement attribute with changes in fair value included in earnings for both servicing rights and certain hybrid instruments. Knowing that the IASB had incorporated a fair value option in IAS 39, *Financial Instruments: Recognition and Measurement*, the Board decided to explore creating a more broadly applicable fair value option. In May 2004, the Board added a project to its agenda to consider whether entities should be permitted a one-time election, at the initial recognition of a contract, to report financial instruments, and perhaps certain nonfinancial instruments that are similar to financial instruments, at fair value with the changes in fair value included in earnings. Work on this project was deferred until the IASB could conclude its reconsideration of possible modifications to the fair value option in IAS 39. In June 2005, the IASB issued *The Fair Value Option*, an amendment to IAS 39.

Basis for Conclusions

Reasons for Permitting a Fair Value Option

A3. The Board decided to permit entities to elect a fair value option for financial assets and financial liabilities for the following reasons:

a. A fair value option would enable entities to avoid reporting volatility in earnings that results from using different measurement attributes in reporting various financial assets and financial liabilities that are related. The effect on earnings from using mixed measurement attributes under U.S. GAAP may not be representative of the economics of the reporting entity's activities. Although special hedge accounting under Statement 133 compensates in part for the mismatch of measurement attributes, only certain hedging relationships can qualify for hedge accounting and only derivatives can be used as the hedging instrument under Statement 133.
b. A fair value option would enable entities to achieve an offset accounting effect for the changes in the fair values of related assets and liabilities without having to apply complex hedge accounting provisions, thereby providing greater simplicity in the application of accounting guidance. A fair value option would enable entities to

avoid the time, effort, and systems needed to document fair value hedging relationships and demonstrate their effectiveness to qualify for continued hedge accounting. That is, rather than designating a fair value hedging relationship, entities could elect to apply the fair value option to the hedged item at its inception. However, the offset resulting from the application of the fair value option is based on the fair value of the entire financial asset or liability and not selected risks inherent in those financial assets or financial liabilities.

c. A fair value option would achieve further convergence with the IASB, which has incorporated a fair value option for financial instruments in IAS 39.

d. A fair value option would expand the use of the fair value measurement attribute for financial instruments. The Board believes fair values for financial assets and financial liabilities provide more relevant and understandable information than cost or cost-based measures. The Board considers fair value to be more relevant to financial statement users than cost for assessing the current financial position of an entity because fair value reflects the current cash equivalent of the entity's financial instruments rather than the price of a past transaction. With the passage of time, historical prices become irrelevant in assessing an entity's current financial position.

Scope

A4. In undertaking the fair value option project, the Board initially planned to address not only financial assets and financial liabilities but also certain nonfinancial assets and nonfinancial liabilities that are similar to financial items. However, the Board decided that additional input was needed from constituents about the use of fair value in accounting for nonfinancial assets and nonfinancial liabilities. The Board decided to split the project into two phases and use the notice for recipients in the Exposure Draft for Phase 1 to solicit information about the potential application of the fair value option to nonfinancial assets and nonfinancial liabilities. Consequently, Phase 1 addresses the fair value option for certain financial assets and financial liabilities, and Phase 2 will consider permitting the fair value option to be elected for certain nonfinancial assets and nonfinancial liabilities and some of the financial assets and financial liabilities excluded from the scope of Phase 1.

A5. The Board discussed whether the fair value option should be permitted for financial assets and financial liabilities that would otherwise not be recognized at inception under existing GAAP. The Board determined that under Phase 1 of the project, the fair value option should be permitted at inception for unrecognized firm commitments that involve only financial instruments. This Statement uses the definition of *firm commitment* as set forth in Statement 133, which requires that the terms of the forward contract include a disincentive for nonperformance that is sufficiently large to make performance probable. The Board notes that Statement 133 Implementation Issue No. F3, "Firm Commitments—Statutory Remedies for Default Constituting a Disincentive for Nonperformance," clarifies that the binding provisions of a firm commitment are regarded to include those legal rights and obligations codified in the laws to which such an agreement is subject.

A6. The Board considered whether the fair value option should not be permitted for certain financial assets and financial liabilities. The Board's discussions focused on items that have historically been excluded from pronouncements addressing financial instruments broadly, particularly the scope exceptions in FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments.* The Board supported a broad application of the fair value option and decided to keep scope exceptions to a minimum. The Board decided to exclude from the scope of this Statement the following financial assets and financial liabilities for the reasons indicated:

a. An investment (principally an investment in a subsidiary) that would otherwise be consolidated. The Board believes the fair value option project should not be used to make significant changes to consolidation practices.
b. Employers' and plans' financial obligations for pension benefits, other postretirement benefits (including health care and life insurance benefits), postemployment benefits, employee stock option and stock purchase plans, and other forms of deferred compensation arrangements as defined in Statements 35, 87, 106, 112, 123 (revised December 2004), 43, and 146, and Opinion 12. The Board believes that any modifications should be part of a reconsideration of those individual areas.
c. Financial liabilities recognized under lease contracts as defined in Statement 13. (This exclusion does not include a contingent obligation arising out of a cancelled lease and a guarantee of a third-party lease obligation.) The Board wanted to avoid undermining the lease accounting provisions of Statement 13 (as amended), which requires measuring the lessee's obligation for a capital lease at an amount that may not be the fair value of that liability. The Board believes those lease accounting provisions should not be changed by the fair value option project without a comprehensive reconsideration of the accounting for lease contracts. The Board believes also that no scope exception is needed for the assets recognized by lessors under sales-type leases, direct financing leases, or leveraged leases because those assets are not purely financial assets and, thus, are not included in the scope of this Statement.
d. Written loan commitments that are not accounted for as derivatives under Statement 133. The Board will include such written loan commitments in the deliberations of Phase 2 because nonfinancial components affect the determination of the fair value of those written loan commitments.
e. Financial liabilities for demand deposit accounts. The Board will include the liability for demand deposit accounts in the deliberations of Phase 2 because nonfinancial components affect the determination of the fair value of those demand deposit accounts.

The Board also affirmed that the election of the fair value option is not permitted for current or deferred income tax assets or liabilities because such assets and liabilities are not contractual and, thus, are not financial assets or financial liabilities.

A7. The Board discussed whether the fair value option election should be prohibited for nonpublic entities that have elected the exception under FASB Statement No. 126, *Exemption from Certain Required Disclosures about Financial Instruments for Certain Nonpublic Entities,* from having to disclose fair values under Statement 107. The Board noted that a significant difference exists between a nonpublic company's election not to be subject to Statement 107, which requires fair value disclosures of *all* of an entity's financial assets and financial liabilities (if practicable), and a nonpublic company's desire to elect the fair value option for selected financial assets and financial liabilities. Because the fair value option election may be applied on a contract-by-contract basis, the Board believes that the fair value option election should be available to nonpublic entities that have elected the Statement 126 exception.

Election of the Fair Value Option

A8. The Board decided that the election of the fair value option should be made at initial recognition of the financial asset or financial liability or upon an event that gives rise to new-basis accounting at fair value for that item. An election after initial recognition would permit entities to recognize gains or losses in earnings after those gains and losses had occurred and, consequently, is not permitted. The Board acknowledged that an entity would need documentation as evidence of compliance, but it decided not to establish specific documentation requirements. Rather, it decided that evidence could be either concurrent documentation or a preexisting documented policy of an automatic election. To provide entities with greater flexibility in obtaining benefits from the fair value option, the Board decided both to permit the election to be made on a contract-by-contract basis and to not prescribe any qualifying eligibility criteria. The Board decided that once an entity elects the fair value option for a financial asset or financial liability, it should not be permitted to subsequently discontinue the use of the fair value measurement treatment for reporting that financial asset or financial liability.

Use of Non-Fair-Value Measures

A9. The Board discussed whether entities should be permitted to elect (outside of the hedge accounting provided in Statement 133) to recognize in earnings the change in an asset's or liability's fair value attributable to only certain selected risks (rather than the total change in fair value). The Board rejected recognizing only fair value changes that are attributable to only selected risks because it was inconsistent with expanding use of the fair value measurement attribute and international convergence. Moreover, the resulting measurement would not represent the fair value of the financial asset or financial liability as a whole.

A10. The Board also considered whether to curtail the debtor's recognizing in earnings the effect of changes in its creditworthiness in reporting liabilities at fair value when the fair value option has been elected. For example, the debtor might exclude the effects of the change in its creditworthiness from the liability's carrying amount, resulting in a non-fair-value measure. The Board agreed that liability remeasurements at fair value should include the effect of changes in creditworthiness so that the estimate reflects the amount that would be observed in an exchange between willing parties of the same credit quality. The majority of Board members concluded that there is no justification, conceptual or otherwise, for curtailing the debtor's recognizing in earnings the effect of changes in its creditworthiness in reporting liabilities at fair value. However, the Board decided to require additional disclosures that would assist users of financial statements in understanding the related reporting. If significant changes in the fair values of financial liabilities for which the fair value option has been elected occur in any period presented, the entity is required to disclose qualitative information about the reasons for those significant fair value changes, which are included in current-period earnings.

A11. Some Board members disagreed with the conclusion that the effect of changes in the issuer's own creditworthiness should be reported as gains and losses in the issuer's financial statements. While conceptually they agreed that the effect of changes in the obligor's creditworthiness is part of the change in the fair value of its liabilities, those Board members believe that recognition of that effect should not be included in financial statements that are prepared using disparate recognition and measurement standards. For example, presumably, a deterioration in the obligor's creditworthiness is caused by some aspect of the obligor's business, such as the loss of a major customer or an impairment of the long-lived assets of the entity. The current accounting model does not necessarily recognize the effects of those events contemporaneously in the financial statements at fair value. Therefore, an offsetting economic "loss" might not be recognized concurrently with the gain on the obligor's liabilities. They also were not convinced that reporting a gain from a deterioration in the obligor's creditworthiness with accretion of the discount in subsequent periods (yielding a higher amount of interest expense), or the inverse for a loss situation, was useful reporting to investors.

Financial Statement Presentation and Disclosures

A12. The Board considered whether any special display guidance for the statement of financial position or additional disclosures were needed to compensate for the lack of comparability that will arise from the use of the fair value option. The Board decided that special display is needed on the statement of financial position with respect to the elective use of fair values. It decided that assets and liabilities that are subsequently measured at fair value pursuant to the election of the fair value option under this Statement should be reported in a manner that separates those reported fair values from the carrying amounts of assets and liabilities subsequently measured using another measurement attribute on the face of the statement of financial position. To accomplish that separate reporting, an entity may either (a) display separate line items for the fair value and non-fair-value carrying amounts or (b) present amounts that aggregate those fair value and non-fair-value amounts and disclose parenthetically the amount of fair value included in the aggregate amount for that line item.

A13. For financial assets and financial liabilities for which the fair value option has been elected, the Board decided to require disclosure of the difference between the carrying amount of any financial liabilities reported at fair value due to election of the fair value option and the aggregate principal amount the entity would be contractually required to pay to the holders of the obligations at maturity (or through the maturity date for any debts whose principal amounts are payable in installments). This disclosure is similar to one required by the IASB and will give users of financial statements relevant information about the relationship between current value and the related required cash payments.

A14. To address concerns about the lack of comparability with respect to reporting in the income statement, the Board decided to require disclosure of information sufficient to allow users of financial statements to understand the effect on earnings of changes in the fair values of the financial assets and financial liabilities subsequently measured at fair value as a result of a fair value election. In addition, the Board decided to require quantitative information by line item indicating where gains and losses are reported in the income statement arising from the changes in the fair value of financial assets and financial liabilities for which the fair value option has been elected.

A15. The Board considered whether guidance should be provided about how reported interest should be determined for receivables and payables reported at fair value under the fair value option. The Board noted that the issue of determining interest when financial assets and financial liabilities are measured at fair value is not new and would best be resolved in a different project. The Board decided to require disclosure of a description indicating how interest and dividends are measured and reported in the income statement.

Cash Flow Reporting

A16. The Board considered whether the cash receipts and cash payments related to financial assets and financial liabilities for which the fair value option has been elected would be required to be classified as operating activities in the statement of cash flows, since that classification is required for trading securities under Statement 115. The Board decided that the required classification as operating activities for trading securities is inappropriate because Statement 115 permits securities to be classified as trading even though they are not being held for sale in the near term. The Board concluded that the cash receipts and cash payments related to trading securities as well as to financial assets and financial liabilities for which the fair value option has been elected should be classified pursuant to Statement 95 (as amended) based on the nature and purpose for which the related financial assets and financial liabilities were acquired or incurred. The Board decided that Statements 95 and 115 as well as FASB Statements No. 102, *Statement of Cash Flows—Exemption of Certain Enterprises and Classification of Cash Flows from Certain Securities Acquired for Resale,* and No. 145, *Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections,* should be amended to reflect those conclusions.

A17. The Board considered amending Statement 95 to require a reconciling line item for changes in fair value when the indirect method is followed in presenting the statement of cash flows, but it decided that amendment would not be necessary because paragraph 29 of Statement 95 requires separate line items for major reconciling items.

Amendments Related to the Fair Value Election

A18. In addition to the amendments of Statements 95, 102, 115, and 145 regarding the classification of the cash receipts and cash payments related to trading securities discussed in paragraph A16, the Board considered whether other amendments were warranted. The Board decided that the special display requirements on the statement of financial position with respect to the elective use of fair values should apply to other areas involving the elective use of fair value measurements with changes in fair value reported in earnings: the three current projects on servicing rights, hybrid financial instruments, and life settlement contracts and the use of the trading category under Statement 115. The Board's decision will be reflected in the final pronouncements on those three projects; however, a further amendment of Statement 115 is warranted to require entities to either display separate line items in an entity's statement of financial position for the fair value and non-fair-value carrying amounts for investments in debt and equity securities or present amounts that aggregate those fair value and non-fair-value amounts provided that the amount of fair value for available-for-sale and trading securities included in the aggregate amount for that line item is separately disclosed parenthetically on the face of the entity's statement of financial position.

Effective Date and Transition

A19. The Board decided that this Statement should be effective as of the beginning of each reporting entity's first fiscal year that begins after December 15, 2006, with earlier adoption permitted as of the beginning of an entity's earlier fiscal year that begins after issuance of this Statement (thereby resulting in an earlier effective date). The Board decided to permit an entity to elect the fair value option for existing financial assets and financial liabilities that are within the scope of this Statement, rather than limit its application to only newly recognized financial assets and financial liabilities. The Board decided that retrospective application of this Statement to fiscal years preceding the effective date should not be permitted. Therefore, the effect of the initial adoption of this Statement attributable to the election of the fair value option for selected financial assets and financial liabilities existing at the effective date should be accounted for as a cumulative-effect adjustment of retained earnings as of the effective date, not the beginning of the earliest year presented.

A20. The Board considered whether to permit election of the fair value option for available-for-sale and held-to-maturity securities previously accounted for under Statement 115. The Board decided to permit an entity to elect the fair value option for those securities upon the initial adoption of this Statement, which has the effect of reclassifying those securities into the trading category. However, the Board decided that the amount of the effect of that reclassification into the trading category should be included in the cumulative-effect adjustment of retained earnings, and the amount of the effect of that reclassification should be separately disclosed. The effect of that reclassification into the trading category arising from the initial adoption of this Statement should not be included in current-period earnings as a transfer between categories under Statement 115.

Similarities and Differences with International Accounting Standards

A21. The IASB has included a fair value option for financial instruments in IAS 39. Its provisions are similar to those in this Statement insofar as the fair value options in both pronouncements require that the election:

a. Be made at the initial recognition of the financial asset or financial liability
b. Is irrevocable

c. Results in the change in fair value being recognized in earnings (referred to as "profit or loss" in IAS 39) as those changes occur.

A22. The differences between the provisions in this Statement and international standards pertain principally to disclosures, scope exceptions, and whether certain eligibility criteria must be met to elect the fair value option.

a. IAS 32, *Financial Instruments: Disclosure and Presentation* (as revised in 2005), requires disclosure of the amount of change during the period and cumulatively in the fair value of the financial instrument that is attributable to changes in credit risk for loans, receivables, and financial liabilities for which the fair value option has been elected. This Statement does not require any disclosures related solely to the portion of a change in fair value attributable to changes in credit risk, although it does require a qualitative disclosure of reasons for significant changes in fair value of financial liabilities.
b. This Statement includes a scope exception for financial liabilities for demand deposit accounts, whereas IAS 39 does not. However, IAS 39 stipulates in paragraph 49 that "The fair value of a financial liability with a demand feature (eg a demand deposit) is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid." The Board will reconsider this scope exception as part of Phase 2 of the fair value option project.
c. This Statement includes a scope exception for written loan commitments that are not accounted for as derivative instruments under Statement 133, whereas IAS 39 does not. The Board will reconsider this scope exception as part of Phase 2 of the fair value option project.
d. This Statement has no eligibility criteria for financial assets and financial liabilities, whereas IAS 39 (as revised in 2005) indicates that, for other than hybrid instruments, the fair value option can be applied only when doing so results in more relevant information either because it eliminates or significantly reduces a measurement or recognition inconsistency (that is, an accounting mismatch) that would otherwise arise from measuring assets or liabilities or recognizing the gains and losses on them on different bases, or because a group of financial assets, financial liabilities, or both is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the entity's key management personnel.

A23. The inability to elect the fair value option for financial liabilities for demand deposit accounts under this Statement would likely not result in a significantly different reporting outcome than election of the fair value option for those liabilities under IAS 39. The extent of the other differences between the FASB and IASB standards related to eligibility criteria will depend on the circumstances and the extent to which entities desiring to elect the fair value option under IAS 39 will be able to meet those criteria.

Benefits and Costs

A24. The mission of the FASB is to establish and improve standards of financial accounting and reporting for the guidance and education of the public, including preparers, auditors, and users of financial information. In fulfilling that mission, the Board endeavors to determine that a proposed standard will fill a significant need and that the costs imposed to meet 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, investors and creditors—both present and potential—and other 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.

A25. The Board's assessment of the benefits and costs of establishing a fair value option was based on discussions with preparers and users of financial statements. The Board considered the costs associated with decreased comparability as a result of allowing a choice between fair value and the non-fair-value measurement attribute otherwise required by GAAP. The Board also considered the benefits arising from mitigating problems of volatility in reported earnings caused by an accounting model that uses multiple measurement attributes; achieving an offset accounting effect for the changes in the fair values of related assets and liabilities without having to apply complex hedge accounting provisions, thereby simplifying the application of accounting guidance; and expanding the use of the fair value measurement attribute for financial instruments. The Board concluded that the financial reporting benefits would outweigh the costs of noncomparability, particularly since the improved disclosures that would be required by this Statement would enable users to compare entities that make different decisions about use of the fair value option.

Alternative Views

A26. One Board member agrees with the observations expressed in paragraph A11 and has additional concerns leading to this alternative view. That Board member believes that most users do not expect revaluation of the entity's debt securities (which are part of an entity's overall capital structure) to recognize deterioration in the entity's own creditworthiness and to be a component of operating performance. In that Board member's view, the value of the entity's overall capital structure (both debt capital and equity capital) should change only to reflect the entity's operations, rather than reflecting the effect of changes in the entity's own creditworthiness. Recognizing that effect in earnings could be misleading to users and potentially misrepresent or conceal operating performance issues. This proposed Statement provides a benefit for the preparer and a cost to the user in understandability and comparability. While that Board member believes the cost-benefit tradeoff is clearly supported for applying the fair value option to assets, it is not clear that this cost-benefit tradeoff is justified for applying the fair value option to the debt portion of an entity's capital structure. At a minimum, eligibility criteria and additional disclosure requirement should be included when the fair value option is elected for the debt portion of an entity's capital structure.

A27. Another Board member disagrees with the Board's decision to permit free choice between different initial and subsequent measurement attributes for certain financial assets and financial liabilities. That Board member agrees with the Board's acknowledgment, in the discussion relating the conclusions in this proposed Statement to the conceptual framework, that the Board's decision impairs comparability and consistency, two desirable qualitative characteristics of financial information in the Board's conceptual framework. Further, that Board member believes that the impairment of comparability and consistency cannot be justified by a cost-benefit analysis. That Board member agrees with the Board's conclusion, as described in paragraph A3, that fair value is a more relevant measurement attribute than cost or cost-based measures for financial assets and financial liabilities.

A28. That Board member believes that treatment alternatives, such as the one provided in this proposed Statement, are inherently undesirable because they are inconsistent with comparability. The Board acknowledges that comparability between entities will be impaired to the extent that different entities that hold similar financial assets and financial liabilities apply different measurement attributes. In addition, because the treatment alternative is applied contract-by-contract within an entity, it will probably result in different measurement attributes for similar financial assets and financial liabilities within an entity. That Board member believes that the disclosures required by this proposed Statement, taken together with disclosure requirements in other GAAP, are not a substitute for consistent and comparable measurement of similar items.

A29. With regard to the cost-benefit criterion of the Board's conceptual framework, that Board member notes that the incremental burden that would be imposed on preparers by a requirement to measure all financial assets and financial liabilities that are within the scope of this proposed Statement initially and subsequently at fair value would not be large, given the requirements of existing accounting guidance. Statement 107 already requires certain fair value measurements for financial instruments, unless those measurements are not practicable. Therefore, the ability to measure many financial assets and financial liabilities at fair value should already be in place. That Board member acknowledges that the scope of this proposed Statement includes several items that are not within the scope of Statement 107, but believes that, if the Board wishes to reduce the incremental burden on preparers, a preferable approach would be to require fair value as a measurement attribute, for recognition purposes, only for those items that are within the scope of Statement 107.

Appendix B

AMENDMENTS TO EXISTING PRONOUNCEMENTS

B1. FASB Statement No. 95, *Statement of Cash Flows*, is amended as follows: [Added text is underlined and deleted text is ~~struck out~~.]

a. Paragraph 15, as amended:

> Investing activities include making and collecting loans and acquiring and disposing of debt or equity instruments and property, plant, and equipment and other productive assets, that is, assets held for or used in the production of goods or services by the enterprise (other than materials that are part of the enterprise's inventory). Investing activities exclude acquiring and disposing of certain loans or other debt or equity instruments that are acquired specifically for resale, as discussed in Statement 102~~, and securities that are classified as trading securities as discussed in FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*~~.

b. Paragraph 16, as amended:

> Cash inflows from investing activities are:[5]
>
> a. Receipts from collections or sales of loans made by the enterprise and of other entities' debt instruments (other than cash equivalents~~,~~ and certain debt instruments that are acquired specifically for resale as discussed in Statement 102~~, and securities classified as trading securities as discussed in Statement 115~~) that were purchased by the enterprise
> b. Receipts from sales of equity instruments of other enterprises (other than certain equity instruments carried in a trading account as described in Statement 102~~, and certain securities classified as trading securities as discussed in Statement 115~~) and from returns *of* investment in those instruments
> c. Receipts from sales of property, plant, and equipment and other productive assets.

c. Paragraph 17, as amended:

> Cash outflows for investing activities are:
>
> a. Disbursements for loans made by the enterprise and payments to acquire debt instruments of other entities (other than cash equivalents~~,~~ and certain debt instruments that are acquired specifically for resale as discussed in Statement 102~~, and securities classified as trading securities as discussed in Statement 115~~)
> b. Payments to acquire equity instruments of other enterprises (other than certain equity instruments carried in a trading account as described in Statement 102

~~and certain securities classified as trading securities as discussed in Statement 115~~)

c. Payments at the time of purchase or soon before or after purchase[6] to acquire property, plant, and equipment and other productive assets.[7]

d. Footnote 8c to paragraph 22:

The term *goods* includes certain loans and other debt and equity instruments of other enterprises that are acquired specifically for resale, as discussed in Statement 102~~, and securities that are classified as trading securities as discussed in Statement 115~~.

B2. FASB Statement No. 102, *Statement of Cash Flows—Exemption of Certain Enterprises and Classification of Cash Flows from Certain Securities Acquired for Resale,* is amended as follows:

a. Paragraph 8, as amended:

Banks, brokers and dealers in securities, and other enterprises may carry securities and other assets in a trading account.[3] Cash receipts and cash payments resulting from purchases and sales of securities classified as trading securities as discussed in FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* shall be classified <u>pursuant to Statement 95 (as amended) based on the nature and purpose for which the securities were acquired</u>~~as operating cash flows~~. Cash receipts and cash payments resulting from purchases and sales of other securities and other assets shall be classified as operating cash flows if those assets are acquired specifically for resale and are carried at market value in a trading account. Cash flows from purchases, sales, and maturities of available-for-sale securities shall be classified as cash flows from investing activities and reported gross in the statement of cash flows.

b. Paragraph 10(b), as amended:

The following sentence is added to the end of paragraph 15:

> Investing activities exclude acquiring and disposing of certain loans or other debt or equity instruments that are acquired specifically for resale, as discussed in Statement 102~~, and securities that are classified as trading securities as discussed in FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*~~.

c. Paragraph 10(c), as amended:

The parenthetical comment in paragraphs 16(a) and 17(a) is superseded by the following:

(other than cash equivalents~~,~~ and certain debt instruments that are acquired specifically for resale as discussed in Statement 102~~, and securities classified as trading securities as discussed in Statement 115~~)

d. Paragraph 10(d), as amended:

The following parenthetical comment is added after the word *enterprises* in paragraphs 16(b) and 17(b):

(other than certain equity instruments carried in a trading account as described in Statement 102~~ and certain securities classified as trading securities as discussed in Statement 115~~)

e. Paragraph 10(e), as amended:

The following footnote is added after the word *goods* in paragraphs 22(a) and 23(a):

*The term *goods* includes certain loans and other debt and equity instruments of other enterprises that are acquired specifically for resale, as discussed in Statement 102~~, and securities that are classified as trading securities as discussed in Statement 115~~.

B3. FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* is amended as follows:

a. Paragraph 17, as amended:

An enterprise that presents a classified statement of financial position shall report individual held-to-maturity securities, individual available-for-sale securities, and individual trading securities as either current or noncurrent, as appropriate, under the provisions of ARB No. 43, Chapter 3A, "Working Capital—Current Assets and Current Liabilities."[5] An enterprise shall report its investments in available-for-sale securities and trading securities in a manner that separates the reported fair values for those securities from the carrying amounts of other assets that are subsequently measured using another measurement attribute on the face of the statement of financial position. To accomplish that separate reporting, an enterprise may either (a) display separate line items for the fair value and non-fair-value carrying amounts or (b) present the aggregate of those fair value and non-fair-value amounts and parenthetically disclose the amount of fair value included in the aggregate amount.

b. Paragraph 18:

> Cash flows from purchases, sales, and maturities of available-for-sale securities and held-to-maturity securities shall be classified as cash flows from investing activities and reported gross for each security classification in the statement of cash flows. Cash flows from purchases, sales, and maturities of trading securities shall be classified based on the nature and purpose for which the securities were acquired~~ as cash flows from operating activities~~.

B4. FASB Statement No. 145, *Rescission of FASB Statements 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections,* is amended as follows:

a. Paragraph 9(f):

> FASB Statement No. 95, *Statement of Cash Flows.*
>
> (1) ~~In the last sentence of paragraph 15, as amended by FASB Statement No. 102, *Statement of Cash Flows—Exemption of Certain Enterprises and Classification of Cash Flows from Certain Securities Acquired for Resale,* the phrase *, and securities that are classified as trading securities as discussed in FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities* is added after *Statement 102.*~~
>
> (2) The parenthetical comment in paragraphs 16(a) and 17(a), as amended by Statement 102, is replaced by the following:
>
> > (other than cash equivalents~~,~~ and certain debt instruments that are acquired specifically for resale as discussed in Statement 102~~, and securities classified as trading securities as discussed in Statement 115~~)
>
> (3) The parenthetical comment in paragraphs 16(b) and 17(b), as amended by Statement 102, is replaced by the following:
>
> > (other than certain equity instruments carried in a trading account as described in Statement 102~~ and certain securities classified as trading securities as discussed in Statement 115~~)
>
> (4) In footnote 5, the following parenthetical comment is added after *debt or equity instruments*:
>
> > (other than cash equivalents~~,~~ and certain debt instruments that are acquired specifically for resale as discussed in Statement 102~~, and securities classified as trading securities as discussed in Statement 115~~)
>
> (5) ~~In the footnote after *goods* in paragraphs 22(a) and 23(a), added by Statement 102, *, and securities that are classified as trading securities as discussed in Statement 115* is added after *Statement 102.*~~

b. Paragraph 9(g):

FASB Statement No. 102, *Statement of Cash Flows—Exemption of Certain Enterprises and Classification of Cash Flows from Certain Securities Acquired for Resale*. Paragraph 8 is amended as follows:

(1) The following sentence is added after the first sentence:

> Cash receipts and cash payments resulting from purchases and sales of securities classified as trading securities as discussed in FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, shall be classified pursuant to Statement 95 (as amended) based on the nature and purpose for which the securities were acquired ~~as operating cash flows~~.

(2) In the second sentence, *other* is added before *securities*.