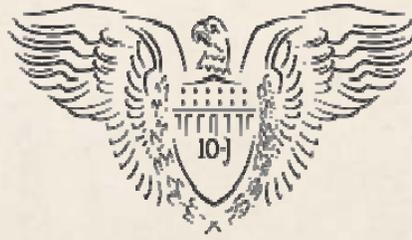


FASB Proposal

Accounting for Financial Instruments



FEDERAL RESERVE BANK *of* KANSAS CITY

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FASB Proposal: Accounting for Financial Instruments

- Proposal:
 - Fair value (FV) balance sheet for most financial instruments, including loans and deposits
 - Exceptions: short-term trade receivables/payables; debt (unless the entity has significant financial assets)
 - Narrowing of equity method (to strategic investments); others at FV
 - Change in fair value recognized in net income unless it qualifies for other comprehensive income. For OCI treatment:
 - Must be held long-term for collection of cash flows
 - Must not have embedded derivatives
 - Equity securities and derivatives do not qualify for OCI
- Comment period closed September 30, 2010
- Responses from federal banking regulators / others
- FASB next steps

FASB Proposal: Accounting for Financial Instruments (Cont'd)

Financial Instrument	Current U.S. GAAP	Proposed U.S. GAAP	Current or Proposed IFRS
Short-Term Receivables / Payables	<ul style="list-style-type: none"> • Amortized Cost 	<ul style="list-style-type: none"> • Amortized cost if criteria met 	<ul style="list-style-type: none"> • Amortized cost if criteria met
Unconsolidated Equity Investment	<ul style="list-style-type: none"> • Fair value through OCI if AFS security • Fair value through net income if trading/fair value election • Equity method • Cost method 	<ul style="list-style-type: none"> • Fair value through net income • Equity method • Redemption value for certain investments that can be redeemed at a specified amount 	<ul style="list-style-type: none"> • Fair value through OCI if not held for trading and election made (includes realized gains/losses through sales/settlements); otherwise, • Fair value through net income
Debt Security	<ul style="list-style-type: none"> • Amortized cost if HTM • Fair value through OCI if AFS • Fair value through net income if trading 	<ul style="list-style-type: none"> • Fair value through OCI if election made and criteria met; otherwise, • Fair value through net income 	<ul style="list-style-type: none"> • Amortized cost if criteria are met and fair value election not made

FASB Proposal: Accounting for Financial Instruments (Cont'd)

Financial Instrument	Current U.S. GAAP	Proposed U.S. GAAP	Current or Proposed IFRS
Loans Receivable	<ul style="list-style-type: none"> • Amortized cost • Fair value through net income if under fair value election • Lower of cost or fair value if held for sale 	<ul style="list-style-type: none"> • Fair value through OCI if election made and criteria met; otherwise, • Fair value through net income 	<ul style="list-style-type: none"> • Amortized cost if criteria are met and fair value election not made
Loan Commitments	<ul style="list-style-type: none"> • Fair value through net income for commitments related to mortgage loans held for sale; otherwise, not recognized • Liability for probable credit exposure recognized 	<ul style="list-style-type: none"> • Treatment consistent with loan type upon funding for those commitments within the scope 	<ul style="list-style-type: none"> • For commitments within scope, treatment depends on terms of instrument and entity's circumstances

FASB Proposal: Accounting for Financial Instruments (Cont'd)

Financial Instrument	Current U.S. GAAP	Proposed U.S. GAAP	Current or Proposed IFRS
Impairment of Financial Assets	<ul style="list-style-type: none"> • Equity securities – full impairment recognized in net income if other than temporary • Debt securities – impairment attributable to credit losses recognized in net income; other impairment recognized through OCI if no intent / likely requirement to sell • Loans receivable and commitments to lend – impairment recognized when probable that a loss has been incurred 	<ul style="list-style-type: none"> • Credit impairment recognized in net income when entity does not expect to collect all contractual amounts due for originated assets or originally expected for purchased assets • Inappropriate to conclude asset is not impaired solely because fair value is greater than amortized cost • If an asset is evaluated individually and deemed not to be impaired, an entity would consider whether, when evaluating assets that have similar characteristics, impairment is indicated 	<ul style="list-style-type: none"> • Expected loss model with initial losses factored in to effective interest rate

FASB Proposal: Accounting for Financial Instruments (Cont'd)

Financial Instrument	Current U.S. GAAP	Proposed U.S. GAAP	Current or Proposed IFRS
Deposits	<ul style="list-style-type: none"> • Amortized cost • Fair value through net income with fair value election 	<ul style="list-style-type: none"> • Core deposit liability subsequently measured at present value of average liability discounted at excess of alternative funds rate over all-in cost to service rate • Changes in re-measurement amount recognized in OCI if criteria met • Noncore deposits – fair value through OCI if election made and criteria met; otherwise, fair value through net income 	<ul style="list-style-type: none"> • Amortized cost if criteria are met and fair value election not made
Debt	<ul style="list-style-type: none"> • Amortized cost • Fair value through net income with fair value election 	<ul style="list-style-type: none"> • Amortized cost if election made and criteria met • Fair value through OCI if election made and criteria met • Otherwise, fair value through net income 	<ul style="list-style-type: none"> • Amortized cost if criteria are met and fair value election not made • Under fair value election, can elect to report change in value attributable to own credit risk in OCI

FASB Proposal: Accounting for Financial Instruments (Cont'd)

Financial Instrument	Current U.S. GAAP	Proposed U.S. GAAP	Current or Proposed IFRS
Hybrid Financial Assets	<ul style="list-style-type: none"> • Embedded derivative bifurcated and recorded at fair value if required under ASC 815 with host contract following accounting applicable to type of host • Entire instrument recognized at fair value through net income under fair value election 	<ul style="list-style-type: none"> • Entire instrument recorded at fair value through net income if derivative would otherwise require bifurcation • If not, can elect OCI if criteria are met 	<ul style="list-style-type: none"> • Consistent with approach for host financial asset
Hybrid Financial Liabilities	<ul style="list-style-type: none"> • Embedded derivative bifurcated and recorded at fair value if required under ASC 815 with host contract following accounting applicable to type of host • Entire instrument recognized at fair value through net income under fair value election 	<ul style="list-style-type: none"> • Entire instrument recognized at fair value through net income if derivative would otherwise require bifurcation • If not, can elect OCI if criteria are met 	<ul style="list-style-type: none"> • Fair value option for entire instrument or separate recognition of embedded derivative