



# Accounting for Securitizations (FAS 166) – Overview

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- Address practices that have developed since the issuance of FAS 140 that are not consistent with its original intent and key requirements
- Clarify certain provisions that have resulted in inconsistencies
- Provide users of financial statements with greater transparency about transfers of financial assets, including a transferor's continuing involvement

- Eliminates qualifying SPE (“QSPE”) concept from Statement 140 and the exception to the consolidation of a QSPE in Interpretation 46(R)
- Modifies the financial components approach
- Introduces the concept of a participating interest
- Clarifies and amends the conditions for derecognition
- Eliminates the special treatment for guaranteed mortgage securitizations
- Changes the initial measurement guidance for transfers of financial assets accounted for as sales
- Requires increased disclosure

- All former QSPEs must be evaluated for consolidation under the applicable consolidation guidance on the effective date and each reporting period thereafter
- Most QSPEs will meet the definition of a variable interest entity and thus will be subject to Interpretation 46(R), as amended by Statement 167

- Limits the circumstances in which a portion of a financial asset is eligible for derecognition
- Transfers of portions of financial assets are eligible for derecognition only if the transferred portions mirror the characteristics of the original financial asset
- Apply the derecognition criteria in paragraph 9 (ASC 860-10-40-5) to EITHER
  - An entire financial asset
  - A group of entire financial assets
  - A participating interest in an entire financial asset
- Deletes the term undivided interest

## **A participating interest has all of the following characteristics:**

- It is a proportionate (pro rata) ownership interest in an entire financial asset
- Except for compensation paid for services performed, all cash flows from the asset are allocated to the participating interest holders in proportion to their share of ownership
- Involves no recourse (other than standard representations and warranties) to, or subordination by, any participating interest holder
- No party has the right to pledge or exchange the entire asset

## **Clarifies and amends how the derecognition conditions must be applied**

- All entities included in the financial statements being presented
- Must consider the transferor's continuing involvement in the transferred financial assets
- All arrangements and agreements made contemporaneously with, or in contemplation of a transfer, even if those arrangements were not entered into at the time of transfer

## **Isolation criteria – paragraph 9(a) or ASC 860-10-40-5(a)**

- Clarifies that analysis must consider the transferor, its consolidated affiliates included in the financial statements being presented, and its creditors
  - An entity designed to make remote the possibility of bankruptcy or other receivership would be excluded from the analysis
- Adds discussion on true sale and non-consolidation opinions
- Interaction with consolidation literature
- Interaction with the FDIC’s regulation on “Treatment by the FDIC as Conservator or Receiver of Financial Assets Transferred in Connection with a Securitization or Participation”

## Transferee's rights to pledge or exchange – paragraph 9(b) or ASC 860-10-40-5(b)

- Existing criteria does not change
  - Each transferee has the right to pledge or exchange the assets it received
  - No condition both constrains the transferee from taking advantage of its right to pledge or exchange and provides more than a trivial benefit to the transferor
- Eliminates references to a QSPE but replaces it with a “look through” provision
  - If the transferee is an entity whose sole purpose is to engage in securitization or asset backed financing activities and that entity is constrained from pledging or exchanging the assets it receives
  - Look through to third-party beneficial interests

## Effective control – paragraph 9(c) or ASC 860-10-40-5(c)

- Clarifies that the evaluation must consider the transferor, its consolidated affiliates, and its agents
- Changed from a rule to a principle and makes existing effective control criterion examples
  - An agreement that both entitles and obligates the transferor to repurchase or redeem transferred financial assets before their maturity (see paragraphs)
  - Both the unilateral ability to cause the holder to return specific financial assets and more-than-trivial benefit attributable to that ability, other than through a cleanup call
- Adds a third example of effective control
  - 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 probably that the transferee will require the transferor to repurchase them
- Consider both direct and indirect effective control

- Eliminates the special treatment for guaranteed mortgage securitizations (GMS) that do not qualify for sale accounting
  - Mortgage loans transferred to a QSPE in a GMS were permitted to be reclassified to securities
  - Transferor could recognize a servicing asset or liability
- Under FAS 166, will only be able to reclassify loans as securities and recognize a servicing asset/liability if the transfer meets the conditions for sale accounting

- Transfer of an entire financial asset or groups of entire financial assets
  - Recognize and initially measure at fair value all assets obtained (including a transferor's beneficial interests) and liabilities incurred
- Transfers of a participating interest
  - Allocate the previous carrying amount of the entire financial asset between the participating interests sold and the participating interest that continues to be held by the transfer based on their relative fair values

- Eliminates the fair value practicability exception
- Amends guidance on changes that result in the transferor's regaining control of financial assets sold (paragraph 55)
  - Eliminates the “change in Status of a QSPE”
  - Add “change in meeting the definition of a participating interest”
- FDIC Notice of Proposed Rule making related to FAS 166/167 (<http://www.fdic.gov/news/news/press/2009/pr09151.html>)
- Updates to the auditing literature
  - AU 9336, *The Use of Legal Interpretations As Evidential Matter to Support Management's Assertion That a Transfer of Financial Assets Has Met the Isolation Criterion in Paragraph 9(a) of Financial Accounting Standards Board Statement No. 140*
- IASB project on derecognition

- Focuses on providing increased disclosures about a transferor's continuing involvement with transferred financial assets
- Disclosures required under FAS 166 are generally consistent with the public company requirements under FSP FAS 140-4 and FIN 46(R)-8
  - FSP is superseded by FAS 166
  - Apply to both public and non public enterprises
  - Requires disclosure about initial fair value measures
- Contains four disclosure objectives and specific required disclosures
- Linked presentation

- Effective in annual periods beginning after November 15, 2009, including
  - Interim periods within that first annual reporting period
  - Interim and annual reporting periods thereafter
- Recognition and measurement provisions are applicable to transfers that occur after the effective date
  - Calendar year-end companies would apply it for transfers that occur after January 1, 2010
- Disclosure provisions are applicable to transfers that occurred both before and after the effective date
- Early application is prohibited
- On and after the effective date, all existing QSPEs must be evaluated for consolidation

# Statement 166 – Codification cheat sheet

	<b>Statement 140, as amended by Statement 166</b>	<b>Codification (exact paragraph references subject to change)</b>
Participating interest	Paragraph 8B	860-10-40-3C-3I
Derecognition	Paragraph 9	860-10-40-5
Implementation guidance	Paragraphs 26-114	Primarily in 860-10-40, except servicing and examples
Sales of financial assets	Paragraph 10-11A	Subtopic 860-20
Secured borrowings and collateral	Paragraph 12	Subtopic 860-30
Servicing	Paragraphs 13-13B	Subtopic 860-50
Extinguishment of liabilities	Paragraph 16	Topic 405
Disclosures	Paragraphs 16A-17	Sections 860-XX-50
Related literature (FSPs, EITFs, FAS 140 Q&A)	Various places	Primarily Sections 860-xx-55