

# FINANCIAL ACCOUNTING SERIES



## ACCOUNTING STANDARDS UPDATE

No. 2011-03  
April 2011

### Transfers and Servicing (Topic 860)

#### Reconsideration of Effective Control for Repurchase Agreements

An Amendment of the *FASB Accounting Standards Codification*®

Financial Accounting Standards Board  
of the Financial Accounting Foundation

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### Reconsideration of Effective Control for Repurchase Agreements

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401 MERRITT 7, PO BOX 5116, NORWALK, CONNECTICUT 06856-5116



Accounting Standards Update 2011-03

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Reconsideration of Effective Control for Repurchase  
Agreements

April 2011

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## Summary

### Why Is the FASB Issuing This Accounting Standards Update (Update)?

The main objective in developing this Update is to improve the accounting for repurchase agreements (repos) and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. The Board continuously monitors capital markets for reports of significant accounting or financial reporting issues to assess whether standard-setting actions are required. During the global economic crisis, capital market participants questioned the necessity and usefulness of the collateral maintenance guidance for the transferor's ability criterion (described below) when determining whether a repo should be accounted for as a sale or as a secured borrowing.

In a typical repo transaction, an entity transfers financial assets to a counterparty in exchange for cash with an agreement for the counterparty to return the same or equivalent financial assets for a fixed price in the future. Topic 860, Transfers and Servicing, prescribes when an entity may or may not recognize a sale upon the transfer of financial assets subject to repurchase agreements. That determination is based, in part, on whether the entity has maintained effective control over the transferred financial assets. One of the relevant considerations for assessing effective control is the transferor's ability to repurchase or redeem financial assets before maturity. Under this criterion, an entity must consider whether there is an exchange of collateral in sufficient amount so as to reasonably assure the arrangement's completion on substantially the agreed terms, even in the event of the transferee's default. That is, in order for the transferor to assert that it maintained effective control over the transferred assets, the transferor must have the *ability* to repurchase the same or substantially the same assets.

The Board determined that the criterion pertaining to an exchange of collateral should not be a determining factor in assessing effective control. The Board concluded that the assessment of effective control should focus on a transferor's contractual rights and obligations with respect to transferred financial assets, not on whether the transferor has the practical ability to perform in accordance with those rights or obligations. The Board also concluded that the remaining criteria are sufficient to determine effective control. Consequently, the amendments remove the transferor's ability criterion from the consideration of effective control for repos and other agreements that both entitle and obligate the transferor to repurchase or redeem financial assets before their maturity.

## Who Is Affected by the Amendments in This Update?

The amendments in this Update apply to all entities, both public and nonpublic. The amendments affect all entities that enter into agreements to transfer financial assets that both entitle and obligate the transferor to repurchase or redeem the financial assets before their maturity. The amendments do not affect other transfers of financial assets.

## What Are the Main Provisions?

The amendments in this Update remove from the assessment of effective control (1) the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms, even in the event of default by the transferee, and (2) the collateral maintenance implementation guidance related to that criterion.

Other criteria applicable to the assessment of effective control are not changed by the amendments in this Update. Those criteria indicate that the transferor is deemed to have maintained effective control over the financial assets transferred (and thus must account for the transaction as a secured borrowing) for agreements that both entitle and obligate the transferor to repurchase or redeem the financial assets before their maturity if all of the following conditions are met:

1. The financial assets to be repurchased or redeemed are the same or *substantially the same* as those transferred.
2. The agreement is to repurchase or redeem them before maturity, at a fixed or determinable price.
3. The agreement is entered into contemporaneously with, or in contemplation of, the transfer.

## How Do the Main Provisions Differ from Current U.S. Generally Accepted Accounting Principles (GAAP) and Why Are They an Improvement?

The amendments in this Update remove from the assessment of effective control the criterion relating to the transferor's ability to repurchase or redeem financial assets on substantially the agreed terms, even in the event of default by the transferee. The Board concluded that this criterion is not a determining factor of effective control. Consequently, the amendments in this Update also eliminate the requirement to demonstrate that the transferor possesses adequate collateral to fund substantially all the cost of purchasing replacement financial assets. Eliminating the transferor's ability criterion and related implementation guidance

from an entity's assessment of effective control should improve the accounting for repos and other similar transactions.

## When Will the Amendments Be Effective?

The guidance in this Update is effective for the first interim or annual period beginning on or after December 15, 2011. The guidance should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted.

## How Do the Provisions Compare with International Financial Reporting Standards (IFRS)?

The IASB's derecognition guidance is provided under IAS 39, *Financial Instruments: Recognition and Measurement*. The consideration of a transferor's ability to repurchase or redeem financial assets transferred on substantially agreed terms, even in the event of default by the transferee, is not required under IFRS. The amendments in this Update improve convergence by eliminating from U.S. GAAP the need to consider this criterion.



# Amendments to the *FASB Accounting Standards Codification*<sup>®</sup>

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## Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–8. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is underlined, and deleted text is ~~struck out~~.

## Amendments to Subtopic 860-10

2. Amend paragraph 860-10-40-24, with a link to transition paragraph 860-10-65-4, as follows:

### **Transfers and Servicing—Overall**

#### **Derecognition**

##### **General**

**860-10-40-1** This Section sets forth the conditions for derecognition of a **transferred financial asset** and is organized as follows:

- a. Subparagraph superseded by Accounting Standards Update No. 2009-16.
- b. Conditions for a sale of **financial assets**
- c. Application of the sale criteria to instruments that have the potential to be assets or liabilities
- d. Circumstances that result in a **transferor** regaining control of assets previously sold
- e. **Repurchase financings.**

##### **> Conditions for a Sale of Financial Assets**

##### **> > Effective Control**

**860-10-40-22** This guidance discusses the condition in paragraph 860-10-40-5(c) that the transferor, its consolidated affiliates included in the financial statements

being presented, or its agents do not maintain effective control over the transferred financial assets or third-party beneficial interests related to those transferred financial assets.

### >>> **Effective Control through Both a Right and an Obligation**

**860-10-40-23** Although paragraph 860-10-40-5 sets forth criteria that must be met to achieve sale accounting, this guidance addresses criteria that must be met for a transfer to fail the condition in paragraph 860-10-40-5(c) through an agreement of the type described in paragraph 860-10-40-5(c)(1) and thus preclude sale accounting and result in accounting for the transfer as a secured borrowing.

**860-10-40-24** 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 paragraph 860-10-40-5(c)(1), 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. To be substantially the same, 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:
  1. The same primary obligor (except for debt guaranteed by a sovereign government, central bank, government-sponsored enterprise or agency thereof, in which circumstance the guarantor and the terms of the guarantee must be the same)
  2. Identical form and type so as to provide the same risks and rights
  3. The same maturity (or in the circumstance of mortgage-backed pass-through and pay-through securities, similar remaining weighted-average maturities that result in approximately the same market yield)
  4. Identical contractual interest rates
  5. Similar assets as collateral
  6. The same aggregate unpaid principal amount or principal amounts within accepted good delivery standards for the type of security involved. Participants in the mortgage-backed securities market have established parameters for what is considered acceptable delivery. These specific standards are defined by the Bond Market Association and can be found in Uniform Practices for the Clearance and Settlement of Mortgage-Backed Securities and Other Related Securities, which is published by the Bond Market Association.

See paragraph 860-10-55-35 for implementation guidance related to these conditions.

- b. Subparagraph superseded by Accounting Standards Update 2011-03. ~~The transferor is able to repurchase or redeem them on substantially the agreed terms, even in the event of default by the transferee. 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. *Substantially all* is not specifically defined in this Topic. Judgment is needed to interpret the term substantially all and other aspects of the condition that the terms of a repurchase agreement not maintain effective control over the transferred financial asset. See paragraph 860-10-55-37 for implementation guidance related to the term substantially all and other aspects of the condition that the terms of a repurchase agreement not maintain effective control over the transferred financial asset.~~
- c. The agreement is to repurchase or redeem them before maturity, at a fixed or determinable price.
- d. The agreement is entered into contemporaneously with, or in contemplation of, the transfer.

**860-10-40-25** With respect to the condition in (a) in the preceding paragraph to maintain effective control under the condition in paragraph 860-10-40-5(c) as illustrated in paragraph 860-10-40-5(c)(1), the transferor must have both the contractual right and the contractual obligation to reacquire securities that are identical to or substantially the same as those concurrently transferred. Transfers that include only the right to reacquire, at the option of the transferor or upon certain conditions, or only the obligation to reacquire, at the option of the transferee or upon certain conditions, generally do not maintain the transferor's control, because the option might not be exercised or the conditions might not occur. Similarly, expectations of reacquiring the same securities without any contractual commitments (for example, as in wash sales) provide no control over the transferred securities.

3. Supersede paragraphs 860-10-40-26 through 40-27, with a link to transition paragraph 860-10-65-4, as follows:

**860-10-40-26** Paragraph superseded by Accounting Standards Update 2011-03. ~~With respect to the condition in paragraph 860-10-40-24(b), even if the probability of ever holding inadequate collateral appears remote, the transferor would not maintain effective control unless the arrangement assures, by contract or custom, that the collateral is sufficient. If a transferor is substantially overcollateralized at the date of transfer but the arrangement does not provide for frequent adjustments to the amount of collateral maintained by the transferor, the transferor would not maintain effective control to preclude sale accounting. That is, a mechanism to ensure that adequate collateral is maintained must exist even in transactions that are substantially overcollateralized (for example, deep~~

discount and haircut transactions) to indicate that the transferor has maintained effective control that would preclude sale accounting for those transactions.

~~860-10-40-27 Paragraph superseded by Accounting Standards Update 2011-03. This guidance does not prescribe that a specific contractual term, such as a margining provision, must be present to meet the sufficient collateral requirement. Simply excluding a margining provision from a repurchase agreement does not change the accounting that results if the maintenance of sufficient collateral is otherwise assured. For example, a contractual provision that a repurchase agreement is immediately terminated should the value of the collateral become insufficient to fund substantially all of the cost of purchasing replacement financial assets would satisfy the requirement in paragraph 860-10-40-24(b).~~

4. Amend paragraph 860-10-55-34, with a link to transition paragraph 860-10-65-4, and paragraph 860-10-55-35, with no link to a transition paragraph, as follows:

## Implementation Guidance and Illustrations

### General

#### > Implementation Guidance

**860-10-55-1** This Section is organized as follows:

- a. Scope
- aa. Consolidation of transferee by transferor
- aaa. Application of the term **transferred financial assets**
- b. Isolation of transferred **financial assets**
- c. **Transferee's** right to pledge or exchange transferred financial assets
- d. Effective control
- e. Application of sale conditions to specific transactions
- f. Classification of transferred debt securities
- g. Recognition of a sale in separate-entity financial statements.
- h. Subparagraph superseded by Accounting Standards Update No. 2009-16.

#### >> Effective Control

**860-10-55-34** The following provides implementation guidance related to the effective control condition and related examples in paragraph 860-10-40-5(c), specifically:

- a. An agreement that both entitles and obligates the transferor to repurchase or redeem transferred financial assets before maturity (see paragraph 860-10-40-5(c)(1)):
  1. Whether securities exchanged are substantially the same
  2. Subparagraph superseded by Accounting Standards Update 2011-03. Collateral maintenance provisions.
- b. An agreement that provides the transferor with the **unilateral ability** to cause the holder to return specific financial assets, other than through a cleanup call (see paragraph 860-10-40-5(c)(2)):
  1. Rights to reacquire (call) transferred assets.
- c. 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.

### > > > **Whether Securities Exchanged Are Substantially the Same**

**860-10-55-35** This guidance addresses criteria that must be met for a transfer to fail the condition in paragraph 860-10-40-5(c) through an agreement of the type described in paragraph 860-10-40-5(c)(1), precluding sale accounting and resulting, instead, in secured-borrowing accounting. The following are examples of whether securities exchanged are substantially the same as discussed in paragraph 860-10-40-24:

- a. The same primary obligor (see paragraph ~~860-10-40-24(a)(1)~~~~860-10-40-24(a)~~). The exchange of pools of single-family loans would not meet this criterion because the mortgages comprising the pool do not have the same primary obligor, and would therefore not be considered substantially the same.
- b. Identical form and type (see paragraph ~~860-10-40-24(a)(2)~~~~860-10-40-24(b)~~). The following exchanges would not meet this criterion:
  1. GNMA I securities for GNMA II securities
  2. Loans to foreign debtors that are otherwise the same except for different U.S. foreign tax credit benefits (because such differences in the tax receipts associated with the loans result in instruments that vary in form and type)
  3. Commercial paper for redeemable preferred stock.
- 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) (see paragraph 860-10-40-24(a)(3)). The exchange of a fast-pay GNMA certificate (that is, a certificate with underlying mortgage loans that have a high prepayment record) for a slow-pay GNMA certificate would not meet this criterion because differences in the expected remaining lives of the certificates result in different market yields.

- d. Similar assets as ~~{add glossary link}~~collateral~~{add glossary link}~~ (see paragraph 860-10-40-24(a)(5)). Mortgage-backed pass-through and pay-through securities must be collateralized by a similar pool of mortgages, such as single-family residential mortgages, to meet this characteristic.

5. Supersede paragraphs 860-10-55-36 through 55-38 and their related heading, with a link to transition paragraph 860-10-65-4, as follows:

#### **>>> Collateral Maintenance Provisions**

~~**860-10-55-36** Paragraph superseded by Accounting Standards Update 2011-03. Paragraph 860-10-40-24(b) provides guidance related to the maintenance of collateral to fund substantially all of the cost of purchasing replacement securities.~~

~~**860-10-55-37** Paragraph superseded by Accounting Standards Update 2011-03. Arrangements to repurchase or lend readily obtainable securities, typically with as much as 98 percent collateralization (for entities agreeing to repurchase) or as little as 102 percent overcollateralization (for securities lenders), valued daily and adjusted up or down frequently for changes in the market price of the security transferred and with clear powers to use that collateral quickly in the event of default, typically fall clearly within that guideline. Other collateral arrangements typically fall well outside that guideline.~~

~~**860-10-55-38** Paragraph superseded by Accounting Standards Update 2011-03. This Subtopic does not contain special provisions for differences in collateral maintenance requirements that exist in markets outside the United States. Market practices and contracts for **repurchase agreements**, sale buybacks, and securities lending transactions can vary significantly from market to market and country to country. For example, in certain markets, it is not customary to provide or maintain collateral in connection with repurchase transactions. In addition, in certain repurchase agreements, the amount of cash lent often is limited to an amount substantially less than 100 percent (for example, 80 percent or less) of the value of the securities transferred under the repurchase agreements because of the level of market and credit risk associated with those transactions. This Subtopic does not provide special provisions for those differences in collateral requirements. Paragraph 860-10-40-5(c)(1) describes an example of effective control if the transfer involves an agreement that both entities and obligates the transferor to repurchase or redeem the transferred financial assets before maturity and all of the requirements of paragraph 860-10-40-24 are met.~~

#### **>> Application of Sale Conditions to Specific Transactions**

~~**860-10-55-43** The following provides implementation guidance regarding the application of the sale conditions in paragraph 860-10-40-5 to certain transactions, specifically:~~

- a. Pass-through, pay-through, and **revolving-period securitizations**
- b. Factoring arrangements
- c. Transfers of receivables with recourse
- d. Securities lending transactions
- e. Repurchase agreements
- f. Wash sales
- g. Dollar rolls
- h. Loan participations
- i. Banker's acceptances and risk participations in them
- j. Subparagraph superseded by Accounting Standards Update No. 2009-16.
- k. Transfers involving certain transferor powers
- l. Transferor option to repurchase individual financial assets
- m. Transfer of a short-term loan made under a long-term credit commitment
- n. Transfer of bad-debt recovery rights.
- o. Subparagraph superseded by Accounting Standards Update No. 2009-16.

6. Amend paragraphs 860-10-55-53 and 860-10-55-55, with a link to transition paragraph 860-10-65-4, as follows:

**> > > Repurchase Agreements**

**860-10-55-51** Paragraphs 860-10-05-19 through 05-21 provide background on repurchase agreements. Repurchase agreements that do not meet all the conditions in paragraph 860-10-40-5 shall be treated as secured borrowings. Under many agreements to repurchase transferred financial assets before their maturity, the transferor maintains effective control over those financial assets. This Subtopic does not specifically define the term *before maturity*. The only meaningful distinction based on required repurchase at some proportion of the life of the assets transferred is between a repo-to-maturity, in which the typical settlement is a net cash payment, and a repurchase before maturity, in which the portion of the financial asset that remains outstanding is indeed reacquired in an exchange. A transferor's agreement to repurchase a transferred financial asset would not be considered a repurchase or redemption before maturity if, because of the timing of the redemption, the transferor would be unable to sell the financial asset again before its maturity (that is, the period until maturity is so short that the typical settlement is a net cash payment).

**860-10-55-52** 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 pledging 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.

**860-10-55-53** 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 they are~~ substantially the same (see paragraph ~~860-10-40-24(a)~~860-10-40-24) securities as those concurrently transferred ~~is assured~~. Therefore, those transactions shall be accounted for as secured borrowings by both parties to the transfer provided all other criteria for effective control have been met.

**860-10-55-54** Whether a transfer of a debt security is accounted for as a sale under this Topic depends on whether the conditions in paragraph 860-10-40-5 are met. In repurchase transactions involving readily obtainable held-to-maturity debt securities, the conditions set forth in paragraph 860-10-40-24 shall be carefully evaluated to determine whether the transaction should be accounted for as a sale or secured borrowing. For example, if the security that is required to be returned has a different maturity or has a different contractual interest rate from the transferred security, the substantially-the-same criterion would not be met. In that circumstance, effective control would not be maintained under the condition in paragraph 860-10-40-5(c) and the transfer would be accounted for as a sale if the other conditions in paragraph 860-10-40-5 are met. Both parties to a repurchase agreement shall use the same conditions in determining the accounting for a repurchase agreement.

**860-10-55-55** If the conditions in paragraph 860-10-40-5 are met, 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 would be accounted for as sales if the conditions in paragraph 860-10-40-5 are met include transfers with agreements to repurchase at maturity, ~~maturity and transfers with repurchase agreements in which the transferor has not obtained collateral sufficient to fund substantially all of the cost of purchasing replacement financial assets.~~

**860-10-55-56** Repurchase agreements that involve an exchange of securities or letters of credit are accounted for in the same manner as securities lending transactions (see paragraphs 860-30-25-7 through 25-8).

7. Add paragraph 860-10-65-4 and its related heading as follows:

**> Transition Related to Accounting Standards Update No. 2011-03, Transfers and Servicing (Topic 860): Reconsideration of Effective Control for Repurchase Agreements**

**860-10-65-4** The following represents the transition and effective date information related to Accounting Standards Update No. 2011-03, *Transfers and Servicing (Topic 860): Reconsideration of Effective Control for Repurchase Agreements*:

- a. The pending content that links to this paragraph shall be effective for the first interim or annual period beginning on or after December 15, 2011.

b. The pending content that links to this paragraph shall be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted.

8. Amend paragraph 860-10-00-1, by adding the following items to the table, as follows:

**860-10-00-1** The following table identifies the changes made to this Subtopic.

<b>Paragraph Number</b>	<b>Action</b>	<b>Accounting Standards Update</b>	<b>Date</b>
860-10-40-24	Amended	2011-03	04/29/2011
860-10-40-26	Superseded	2011-03	04/29/2011
860-10-40-27	Superseded	2011-03	04/29/2011
860-10-55-34	Amended	2011-03	04/29/2011
860-10-55-35	Amended	2011-03	04/29/2011
860-10-55-36 through 55-38	Superseded	2011-03	04/29/2011
860-10-55-53	Amended	2011-03	04/29/2011
860-10-55-55	Amended	2011-03	04/29/2011
860-10-65-4	Added	2011-03	04/29/2011

*The amendments in this Update were adopted by the unanimous vote of the seven members of the Financial Accounting Standards Board:*

Leslie F. Seidman, *Chairman*  
 Daryl E. Buck  
 Russell G. Golden  
 Thomas J. Linsmeier  
 R. Harold Schroeder  
 Marc A. Siegel  
 Lawrence W. Smith

# Background Information and Basis for Conclusions

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## Introduction

BC1. The following summarizes the Board's considerations in reaching the conclusions in this Update. Individual Board members gave greater weight to some factors than to others.

BC2. The Board concluded that the objective of the amendments should be to improve the assessment of effective control for repos and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity.

BC3. The Board concluded that the criterion that a transferor of financial assets must have the ability to repurchase or redeem those financial assets on substantially the agreed terms, even in the event of default by the transferee (transferor's ability criterion), is not a determinant of effective control. Thus, the Board concluded that these amendments improve the current guidance by removing in its entirety the criterion and its related implementation guidance from Subtopic 860-10.

BC4. The amendments affect only the guidance for repo transactions and other agreements that both entitle and obligate the transferor to repurchase or redeem financial assets before their maturity. The amendments do not affect other criteria that must be satisfied to conclude that sale accounting treatment for transferred financial assets is appropriate.

## Background Information

BC5. A transferor may maintain effective control over transferred financial assets if there is an agreement that both entitles and obligates the transferor to repurchase the financial assets before their maturity. The guidance, before being amended by this Update, stated that a transferor maintained effective control of transferred assets under an agreement that both entitles and obligates the transferor to repurchase or redeem transferred assets if and only if all of the following criteria were met:

- a. The assets to be repurchased or redeemed are the same or substantially the same as those transferred.
- b. The transferor is able to repurchase or redeem them on substantially the agreed terms, even in the event of default by the transferee (transferor's ability criterion).

- c. The agreement is to repurchase or redeem them before maturity, at a fixed or determinable price.
- d. The agreement is entered into contemporaneously with, or in contemplation of, the transfer.

The above criteria are summarized from Topic 860.

BC6. When the guidance in paragraph BC5 was established, the Board concluded as part of the redeliberations of FASB Statement No. 125, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, that the notion of effective control should consider facts and circumstances that go beyond the assessment of legal isolation. The Board based the conclusion, in part, on observation of contracts and practices that prevail in the repo and securities lending markets.

BC7. At that time, the Board concluded that to maintain effective control the transferor must have *both* the contractual right *and* the contractual obligation to reacquire securities that are identical to or *substantially the same* as those concurrently transferred. Furthermore, the Board concluded the transferor's performance of its right to repurchase is not assured unless it is protected by obtaining collateral sufficient to fund substantially all of the cost of purchasing identical replacement securities during the term of the contract.

BC8. Capital market participants raised concerns about whether the collateral maintenance guidance on the transferor's ability criterion was useful and necessary for an entity to determine whether it maintained effective control over financial assets transferred because the accounting results obtained because of that guidance may not faithfully represent the underlying economics of the transaction.

BC9. In response to those concerns, in July 2010, the chairman added a narrowly focused project to the Board's agenda to improve the accounting for repurchase agreements and other agreements that both entitle and obligate the transferor to repurchase or redeem financial assets before their maturity. The Board determined that this project would focus on reconsidering particular aspects of the effective control guidance for those transactions. Specifically, the Board focused on the transferor's ability criterion and the related collateral maintenance guidance.

BC10. The Board issued an Exposure Draft of a proposed Update, *Transfers and Servicing (Topic 860): Reconsideration of Effective Control for Repurchase Agreements*, on November 3, 2010. The Board received 19 comment letters on the Exposure Draft. Most respondents agreed with the Board's proposal to remove the transferor's ability criterion from the assessment of effective control for agreements that both entitle and obligate the transferor to repurchase or redeem transferred financial assets from the transferee. Others disagreed with some aspects of the proposal. The Board considered those comments during its redeliberations of the Exposure Draft at a public meeting held in March 2011.

## Reconsideration of Effective Control

BC11. The Board initially developed the notion of effective control to consider facts and circumstances beyond the assessment of legal isolation to examine the substance (as opposed to the legal form) of what has been agreed upon between the parties to a contract. The Board concluded that this is an important step in determining whether an entity should derecognize financial assets transferred. However, the Board reconsidered whether the presence or absence of collateral maintenance agreements should determine whether the transfer of a financial asset should be treated as a sale or secured borrowing when the other indicators of effective control are met.

BC12. The Board concluded that the transferor's ability criterion and its related implementation guidance about collateral maintenance agreements should be removed entirely from the assessment of effective control and that the transferor's ability criterion is not a determining factor of effective control. The Board determined that the assessment of effective control is sufficiently addressed by retaining the remaining existing guidance, including the other three criteria stated in paragraph BC5.

BC13. The Board considered that the transferor's ability criterion demonstrates an entity's protection and assurance of the ability to perform in accordance with its contractual rights. The Board concluded that an entity's protection and assurance of its ability to perform in accordance with its contractual rights or satisfy its contractual obligations should not be a determining factor as to whether an entity has (or does not have) effective control. The Board also considered that the collateral obtained in a repo transaction is typically cash, which is fungible. The existence or nature of collateral provides no direct or relevant information about an entity's control over financial assets transferred.

BC14. Some respondents to the proposed Update, primarily managers or service providers of funds registered under the Investment Company Act of 1940, raised concerns about the proposed Update's application to mortgage dollar-roll agreements. Specifically, entities with registered funds were concerned about (a) inconsistent application of the remaining guidance and (b) the effect the Update would have on key performance metrics assessed by investors in registered funds.

BC15. Registered funds were concerned that the removal of the transferor ability criterion and the related collateral maintenance guidance could introduce inconsistent application of the remaining guidance to economically similar transactions. Under the previous guidance, many entities only assessed the insufficiency of the collateral obtained as part of the transferor ability criterion to determine that the transferor did not maintain effective control over the financial assets transferred. Registered funds asserted that the removal of this criterion would require all entities to assess whether the financial assets redeemed or repurchased are substantially the same as those transferred. Registered funds

said that this could create potential complexities and inconsistent application because the criteria are subjective and require judgment when determining whether financial assets redeemed or repurchased are substantially the same as those transferred.

BC16. The Board considered these concerns and concluded that (a) the existing guidance to determine whether financial assets redeemed or repurchased are substantially the same as those transferred is sufficient and (b) the effect that the changes could have on registered funds' performance metrics would be appropriate. The Board concluded that it wanted to improve the assessment of effective control for transactions like mortgage dollar rolls. That is, some mortgage dollar rolls were an example of a transaction that might otherwise have been accounted for as a secured borrowing if not for the deleted criterion that is not a determinate of effective control.

## Other Considerations

BC17. Some respondents to the proposed Update asked the Board to also consider amending other guidance in Topic 860. Those requests ranged from the consideration of a new derecognition model to targeted amendments including additional disclosures.

BC18. The Board considered those requests and concluded that each was beyond the narrow scope of this project, which addressed capital market participants' concerns about whether the transferor's ability criterion and the related implementation guidance are useful and necessary for an entity to determine if it maintains effective control over the financial assets transferred. Furthermore, the Board considered that a post-implementation review of the recent changes to Topic 860 due to FASB Statement No. 166, *Accounting for Transfers of Financial Assets*, has not been performed. Therefore, the Board concluded that it would be appropriate to consider making additional significant changes to Topic 860 as part of that review.

## Effective Date and Transition

BC19. The Board included in the proposed Update an effective date for fiscal years, and interim periods within those years, beginning with the first interim or annual period following issuance of the final Update. Some respondents to the proposed Update informed the Board that significant changes to accounting systems were necessary to implement the amendments and that the proposed effective date would be burdensome and impose significant costs.

BC20. The Board considered this feedback and concluded that the amendments in this Update should be effective for the first interim or annual period beginning on or after December 15, 2011. The Board concluded that this effective date will

provide sufficient time for preparers to analyze, apply, and implement the amendments while still providing a timely response to capital market participants' concerns.

BC21. The amendments in this Update prohibit early adoption. The Board concluded that providing alternatives on when entities adopt new guidance decreases the comparability of information presented, thereby increasing the cost of analyzing and using that information. For example, the potential changes in expense ratios for entities with registered funds potentially could reduce comparability between those entities that choose to early adopt and those that do not.

BC22. The Board concluded that, for the transactions covered by the amendments in this Update, the costs of a full retrospective application would outweigh the benefits of providing the information for users of financial statements. Most repo agreements are short term, such that most repo agreements initiated before this Update would no longer be outstanding at the effective date. Therefore, the Board concluded that the amendments should be applied prospectively to both transfers that occur after the effective date and existing transactions that are modified after the effective date. The amendments should be applied on a transactional basis, regardless of whether the transaction is subject to a master netting arrangement.

## Benefits and Costs

BC23. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Board's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC24. While the Board acknowledges that some entities may incur costs as a result of the amendments in this Update, the Board decided that the improvements provided by those amendments outweigh the costs incurred.

## Amendments to the XBRL Taxonomy

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The following elements or modifications to existing elements are proposed additions to the XBRL U.S. GAAP Financial Reporting Taxonomy. They reflect the amendments to the disclosure and presentation requirements of the Accounting Standards Codification and would be used in association (tagged) with the appropriate reported values in the SEC filer XBRL exhibit. Elements that currently exist in the 2011 Taxonomy are marked with an asterisk\* and have been **bolded**. If an existing element was modified, it has been marked to reflect any changes.

Element Name	Standard Label	Definition	Codification Reference
RepurchaseAgreementsPolicyForMonitoringOfMarketValueOfUnderlyingAssets*	Repurchase Agreements, Policy for Monitoring of Market Value of Underlying Assets	<p><del>This describes the entity's provisions to ensure that the cash or other collateral received is sufficient to fund substantially all of the cost of purchasing replacement assets from others.</del></p> <p><u>This describes the entity's provisions to ensure that the market value of the underlying assets remains sufficient to protect the entity in the event of default by the counterparty.</u></p>	235-10-S99-1 <del>860-10-40-24</del>
AccountingStandardsUpdate201103Member	Accounting Standards Update 2011-03	Accounting Standards Update 2011-03 Transfers and Servicing	860-10-65-4

Element Name	Standard Label	Definition	Codification Reference
	[Member]	(Topic 860): Reconsideration of Effective Control for Repurchase Agreements.	