



Financial Accounting
Standards Board

PURPOSE OF THIS STUDY

This study summarizes the results of the FASB staff's review of the application by the Fortune® 1000 companies (with years ended after December 15, 2000) of the new securitization and collateral disclosures required by paragraph 17 of FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. All of the 10-K's and annual reports received by the FASB library were reviewed to determine whether Statement 140 disclosures were made in the companies' financial statements and footnotes. The staff reviewed 763 financial statements, excluding the 237 companies with years ended before December 16, 2000 or whose annual reports were, for some reason, not received by the library.

The document consists of three sections:

- Policy footnotes
- Securitization disclosures
- Secured borrowings and collateral disclosures.

POLICY FOOTNOTES

Most Fortune® 1000 companies did not present the securitization-related disclosures in their financial statements and footnotes. Possible reasons could be that these companies (1) did not participate in securitization transactions or (2) assessed their level of participation in such transactions as immaterial. However, 182 of the Fortune® 1000 companies listed Statement 140 as a newly adopted accounting policy in the company's Management's Discussion and Analysis (MD&A) section or in the company's "summary of significant accounting policy" (SAP) footnote or in both.

Of those companies that did report Statement 140 as a new accounting pronouncement, the Statement 140 disclosures can generally be categorized as disclosures regarding:

- Statement 140 applicability (without specific disclosures)
- Secured borrowings
- Collateral
- Securitization programs
- Retained interests in securitizations.

The staff noted 30 companies that mentioned the applicability of Statement 140 in their MD&A and/or in their SAP but failed to provide any of the disclosure required by Statement 140. Reasons for such action could be:

- Non-applicability of the required footnote disclosures
- Non-materiality of Statement 140 related transactions
- Non-compliance on the part of the company.

SECURITIZATION DISCLOSURES

	Securitization Disclosures		Total
	Yes	No	
Financial Institutions			
Banks	22	7	29
Thrifts	5	4	9
Specialty Finance	8	0	8
Insurance	2	7	9
Broker-Dealers	<u>1</u>	<u>5</u>	<u>6</u>
	38	23	61
Other Companies			
Companies That Said They Securitize Financial Assets	15	2	17
Companies That Disclosed Trade Receivables Sales Programs	0	64	64
Other	<u>0</u>	<u>40</u>	<u>40</u>
	15	106	121
TOTAL COMPANIES*	53	129	182

*Only includes companies that referred to Statement 140 somewhere in their 10-K.

Disclosures by Financial Institutions

In this study, *financial institutions* includes commercial banks, thrifts, finance companies, insurance companies, and broker-dealers.

While the majority of financial institutions referred to Statement 140 in their financial statements, a few large financial institutions made no mention of Statement 140. Also, most insurance companies and broker-dealers did not present the paragraph 17(f) and paragraph 17(g) securitization disclosures.

Disclosures of Accounting Policy and Characteristics of Securitizations

The reference made by most securitizing financial institutions was in the SAP footnote and usually contained the accounting policy disclosures (paragraph 17(f)(1) and paragraph 17(g)(1)) and sometimes the disclosure describing “the characteristics of securitizations” (paragraph 17(f)(2)). Most financial institutions distinguished between the paragraph 17(f)(1) and paragraph 17(g)(1) disclosures using a format similar to the examples in paragraph 343 and paragraph 344, others stated their general policy for measuring retained interests. The other securitization disclosures required by Statement 140 were typically reported in a separate footnote dedicated to securitizations.

Some financial institutions did not make all the required disclosures, saying that the disclosures were “not applicable” or “immaterial.” For example, one regional bank had a securitization footnote, but the company reported that it did not account for its securitizations as sales, while another regional bank mentioned the applicability of Statement 140 but stated that it did not participate in securitization transactions.

Disclosures of Key Assumptions

Most financial institutions explicitly presented the paragraph 17(f)(3) and paragraph 17(g)(2) disclosures about key assumptions used in measuring retained interests. The key assumptions were typically displayed by type of loan, which appears to make the disclosures for specific types of loans more comparable for financial statements users. Companies that followed the format in paragraph 345 and paragraph 346 provided the key assumption information in an easy-to-use and easy-to-understand format. However, the staff found the disclosures by some companies difficult to use, compare, and understand, because the companies created their own disclosure formats and often disclosed information not required by Statement 140. Also, in addition to making the required disclosures, some companies chose to make further disclosures. For example, one financial institution included a chart listing the components of securitization income in order to represent the securitization income as if the receivables had not been sold but remained on the balance sheet.

Loan categories for which paragraph 17(f)(3) and paragraph 17(g)(2) “key assumptions” disclosures were made included:

Consumer	Commercial	Other
Credit Card	Small Business Administration	Municipal Securities
Automobile	Commercial	CLO/CDO*
Recreational Vehicle/Boat	Financial	-
Aircraft	Industrial	-
Manufactured Housing	Commercial Equipment	-
Residential Mortgage	Financing Lease Receivable	-
Jumbo Residential Mortgage	Franchise Receivable	-
Home Equity	Mortgage	-
Student/Education	-	-
Other Unsecured	-	-

*Commercial Loan Obligations/Commercial Debt Obligations

While some financial institutions chose to further segregate loans by categories such as “fixed-rate” and “adjustable-rate” mortgage loans or “Government Sponsored Enterprise” (GSE) and “non-GSE” loans, other financial institutions chose to aggregate specific loans into broad categories such as “consumer” and “commercial.”

Aggregating the various types of loans into overly broad categories made the information more difficult to use, because that makes the comparison between companies and the understanding of the details of specific portfolios very difficult. For example, aggregated disclosure for one company’s “consumer loans” included automobile loans, credit card receivables, and residential mortgages. The FASB staff’s view is that there is little reason to believe that such loans have similar economic characteristics. This view is supported by the actual data presented. For example, the company’s weighted average life of its consumer loans was “6 months–12.6 years.”

Also, some financial institutions chose to disclose assumptions by categories of types of securities held such as “seller interest,” “interest only strips,” “principal only,” “real estate mortgage investment conduits,” and “mortgage servicing rights,” in lieu of segregating the assumptions by underlying loan type. When presented in this format, the securities pertained to only one asset class (for example, residential mortgages). This information seems to be more useful than simply aggregating retained interests by type of loan.

Lastly, although most companies made disclosures regarding their expected static pool losses as required by paragraph 17(g)(2), the information was not provided in the format as modeled in paragraph 347.

Disclosures of Cash Flow

Most companies provided the cash flow disclosures required by paragraph 17(f)(4) and illustrated in paragraph 348, but the majority of those companies did not separate the cash flow information between transferor and special-purpose entity by major asset type as required by paragraph 17(f). Perhaps that is because they closely followed the example in paragraph 348, which did not break out different asset types.

Disclosures of Sensitivity Analysis

Most financial institutions followed the example in paragraph 346 and used a 10 percent and 20 percent adverse change for the sensitivity analysis on retained interests disclosure (paragraph 17(g)(3)). However, a few of the financial institutions used specific changes for various expected levels ranging from a 10-basis-point change to a 200 percent change depending on the key assumption. While most financial institutions only used two adverse change scenarios, a few financial institutions used two increasing and two decreasing changes in expected levels. However, no financial institution used more than the minimum two hypothetical unfavorable variations for each key assumption.

Disclosures of Managed Assets

The staff noted five financial institutions that did not appear to comply with the “managed asset” disclosures required by paragraph 17(g)(4). Although one of the noncompliant companies disclosed managed asset information in the MD&A section of their annual reports, MD&A is unaudited and is therefore not part of the audited financial statements. The other four institutions did not report the information at all.

Also, the staff noted that some companies that reported on managed assets created their own format as opposed to following the illustration in paragraph 349. In some instances, this information appears more useful. For example, one company segregated the managed asset disclosure into “loans owned” and “loans securitized and sold,” and provided the required static pool disclosures for each segment, not just in aggregated form.

Other Observations

Most of the financial institutions that reported mortgage servicing rights (MSR) had the required “MSR disclosures” (paragraph 17(e)) and had the paragraph 17(f) and paragraph 17(g) disclosures for retained interest, the sensitivity analysis disclosure. However, some companies neglected the paragraph 17(f) and paragraph 17(g) disclosures for retained interests. Practically speaking, the key disclosure omitted was the sensitivity analysis.

Non-financial Companies

Two types of non-financial companies appeared to disclose information about securitization: companies that sell trade receivables and companies that securitize other financial assets.

Companies with Trade Receivables Sales Programs

The majority of the companies that had disclosures related to Statement 140 were companies in various industries that sold “trade receivables.” Although these companies disclosed information regarding the “transfer of financial assets,” the companies seem to take the position that they are not subject to the required disclosures in Statement 140. This appears to be technically correct because no “securities” (as defined in FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*) are created in their trade receivable “sales/securitization” transactions, which are typically commercial paper conduit transactions.

Companies that Securitize Other Financial Assets

Of the non-financial companies that securitize other financial assets, the companies either disclosed all the information required by paragraph 17(f) and paragraph 17(g) or they mentioned Statement 140 and reported that securitization transactions were immaterial. The majority of the disclosures of the typical non-financial companies that securitize financial assets followed the format of the examples in Statement 140, paragraphs 343–349, and were easy to understand and use.

Classification in Financial Statements

Most nonfinancial companies classified the costs and cash flows associated with the sales/securitization program as operating income (expense) and operating activities, respectively. However, a number of companies, apparently incorrectly, classified their securitization gains (losses) as interest income (expense) or failed to classify the securitization cash flows in a manner consistent with the requirements of FASB Statements No. 95, *Statement of Cash Flows*, and No. 102, *Statement of Cash Flows*—

Exemption of Certain Enterprises and Classification of Cash Flows from Certain Securities Acquired for Resale, or did both. For example, paragraph 22(a) of Statement 95 specifically requires that proceeds arising from trade receivables transfers be classified as operating cash flows.

SECURED BORROWINGS AND COLLATERAL DISCLOSURES

Secured Borrowings

Of all the companies observed, only three provided a footnote to the financial statements that described their securitization transactions not accounted for as sales as secured borrowings.

Collateral Disclosures

The staff noted that 11 companies devoted an entire footnote to the collateral disclosures required by paragraph 17(a) in addition to providing a description of collateral-related transactions in their SAP. Most of the 11 companies that made disclosures about collateral were broker-dealers. Most of those companies reported that they have pledged assets as collateral and have, accordingly, reclassified and separately reported those assets in the statement of financial position pursuant to paragraph 15(a).

CONCLUSIONS

The companies analyzed appear to be disclosing most of the information required by Statement 140. However, in my opinion, a number of improvements could be made to at least some of the companies' disclosures.

Companies disclosing information about securitization should consider that:

- Aggregation of dissimilar loan types for purposes of the key assumption information makes the disclosures difficult to interpret.
- Disclosing the cash flows between the transferor and special-purpose entity by major asset type is required by Statement 140, paragraph 17(f)(4).
- Disclosing a sensitivity analysis for valuation of servicing rights that are retained interests is required by Statement 140, paragraph 17(g)(3).
- Disclosing information about managed assets in the MD&A section is insufficient to comply with Statement 140. Managed asset disclosures must be incorporated in the audited financial statements.
- Classification of gain (loss) on sale as interest income (expense) and investing activities, respectively, is inconsistent with the requirements of Statements 95 and 102.

The views expressed in this document are those of the author. Official positions of the FASB are determined only after extensive due process and deliberations.