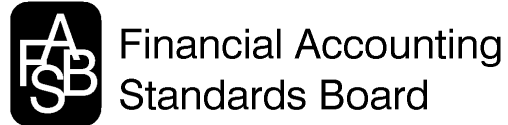


## MINUTES



**To:** Board Members

**From:** Statement 140 Team  
(Cizek, ext. 354, Yust, ext. 442)

**Subject:** Minutes of the June 4, 2008 Board Meeting: Accounting for Interests Held by the Transferor **Date:** June 13, 2008

**cc:** Golden, MacDonald, Bielstein, Donoghue, Lusniak, Mayer, Zecher, Barker, Proestakes, Stocklosa, Nickell, Roberge, C. Smith, Cizek, Reager, Gabriele, Glotzer, Mechanick, Sutay, Posta, Chookaszian, Cosper, Leisenring, Lott, Klimek, Allen, FASB Intranet

*The Board meeting minutes are provided for the information and convenience of constituents who want to follow the Board's deliberations. All of the conclusions reported are tentative and may be changed at future Board meetings. Decisions become final only after a formal written ballot to issue a final Statement, Interpretation, or FASB Staff Position.*

Topic: Accounting for Interests Held by the Transferor

Basis for Discussion: Board Memorandum No. 89

Length of Discussion: 9:00 a.m. to 9:40 a.m.

Attendance:

Board members present: Batavick, Crooch, Herz, Linsmeier, Seidman, L. Smith, and Young

Board members absent: None

Staff in charge of topic: Donoghue

Other staff at Board table: FASB: Golden, Mayer, Barker, Zecher, Lusniak, C. Smith, Cizek, and Yust

## Summary of Decisions Reached

At the June 4, 2008 meeting, the Board discussed several topics as a part of the short-term project to amend FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, and FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities*. For Statement 140, the Board first decided to postpone voting on a rule that sets a minimum third-party investment threshold to recognize a sale of a transferred financial asset. The Board will redeliberate this issue when it concludes on whether and how to amend the consolidation model in Interpretation 46(R). Secondly, the Board deliberated exceptions for a guaranteed mortgage securitization (GMS) that require a transferor to recharacterize a mortgage loan to a security and to recognize a servicing asset or liability as a result of a securitization in which the transfer does not meet the requirements for sale accounting and in which the transferor retains all of the resulting securities. The Board decided to delete the exception that requires a transferor to reclassify interests received in a GMS transaction if the transfer does not qualify as a sale. The Board also decided to remove the exception for GMS transactions currently in Statement 140 that requires a transferor to recognize a servicing asset or liability if the transfer does not qualify as a sale.

## Objectives of Meeting:

One objective of the meeting was to decide whether to require a minimum third-party investment in transferred financial assets for sale accounting in Statement 140. Another objective was to decide whether to continue an exception (1) that requires the reclassification of mortgage loans to securities subsequent to a securitization that does not meet the requirements for sale accounting and (2) that requires the recognition of related servicing assets and liabilities when a securitization of mortgage loans does not meet the requirements for sale accounting. The objectives of the meeting were met.

Matters Discussed and Decisions Reached:

**Issue 1: Minimum Third-Party Investment in a Transferred Financial Asset**

1. Ms. Donoghue noted that with the Board's recent decision to eliminate the qualifying special-purpose entity (QSPE), transferees that are variable interest entities would now be subject to consolidation under Interpretation 46(R). As a result, the current QSPE requirement that at least 10 percent of the beneficial interests be held by parties that are not consolidated by a transferor to meet the requirements for sale accounting will be eliminated. Conceivably, an entity could therefore transfer assets into an entity and take back 100 percent of the interests in those assets and recognize a sale. However, it is unlikely that an entity taking back 100 percent of interests in the asset would pass the amended sale accounting requirements for isolation and effective control.
2. **Staff Recommendation:** The staff recommended that Statement 140 should not have a rule that sets a minimum amount of beneficial interests that must be held by parties other than the transferor and its consolidated affiliates for transfers to meet the requirements for sale accounting.
3. **Board Vote:** Messrs. Batavick and Smith and Ms. Seidman stated that they believed this issue should be addressed by Interpretation 46(R) and that a minimum threshold should not be included in Statement 140. Messrs. Linsmeier, Crooch, Herz, and Young stated that they were concerned that Interpretation 46(R) would not be sufficient and believed a minimum threshold may be appropriate in Statement 140. As the amended Interpretation 46(R) model was not complete, Mr. Herz and Mr. Linsmeier stated that the staff should wait until the Board had voted on a final Interpretation 46(R) model, and then the staff should bring this issue back for discussion.
4. **Board Comments:** Mr. Herz stated that 10 percent seemed like a low threshold and questioned whether it would make sense to account for a transfer as a sale if, for example, the transferor took back 90 percent of the beneficial interests. Ms.

Donoghue noted that a transferor would still have to meet the criteria in paragraph 9 of Statement 140 and avoid consolidation in Interpretation 46(R). Ms. Donoghue also noted that any threshold would be an arbitrary number and is unrelated to the other criteria for sale accounting. Mr. Smith agreed that it was very unlikely that a transferor could avoid consolidation if it took back 90 percent of the beneficial interests and therefore would be eligible for derecognition treatment. Mr. Herz responded that he was concerned a third party could hold a 2 percent residual interest and be considered the primary beneficiary. In this situation, the transferor may achieve sale accounting for the transferred assets.

5. Ms. Seidman noted that any transfer into an entity that is not a QSPE is not currently required to have a minimum amount of beneficial interests held by a nonconsolidated party.
6. Mr. Young stated that he is concerned because the passivity requirements associated with QSPEs would be eliminated along with the minimum third-party investment threshold. Mr. Smith expressed concerns about the amended isolation test. Mr. Herz agreed with Mr. Smith's statements. However, he believes that the pending amendments to Interpretation 46(R) are likely to resolve these concerns. Ms. Seidman added that it may be premature to consider the threshold issue as a backstop to the consolidation model in Interpretation 46(R).

## **Issue 2: Guaranteed Mortgage Securitization Exception**

7. Ms. Donoghue described the history behind the exception provided to GMSs, which require reclassification of loans to securities even when a transferor takes back 100 percent of the loans as a result of a securitization that does not meet the requirements for sale accounting. This exception originated in FASB Statement No. 65, *Accounting for Certain Mortgage Banking Activities*, and has been carried forward through other accounting guidance since the issuance of that document. The reclassification often triggers gain recognition by a transferor. In practice, this exception has sometimes been applied by analogy to financial assets that are not mortgage loans resulting in diversity in the accounting for such transactions.

8. **Staff Recommendation:** The staff recommended that the Board remove the exception that allows for reclassification of loans to securities even when a transferor takes back 100 percent of these securities in GMSs. The staff also recommended that the Board remove the rule in FASB Statement No. 156, *Accounting for Servicing of Financial Assets*, which allows entities to record a servicing asset as a part of a guaranteed mortgage securitization transaction when an entity receives back 100 percent of the securities.
9. **Board Vote:** The Board unanimously voted to remove the exception for GMSs, which allows entities to reclassify loans as securities when a transferor takes back 100 percent of the securities. The Board also unanimously voted to remove the requirement that entities shall recognize a servicing asset or liability for such GMSs.
10. **Board Comments:** Ms. Seidman commented that the implication of this decision is that entities will now account for transferred loans according to current accounting guidance that includes the option to initially report loans at fair value. Ms. Donoghue added that this change would take away the ability for entities to time a gain by securitizing loans at will, thus achieving reclassification and possibly gain recognition.
11. Mr. Herz stated that this exception allowed for entities to obtain a third-party guarantee, often by a government agency, and receive back essentially the same assets and recognize a gain. Ms. Donoghue clarified that Statement 140, unlike Statement 65, required that the securitization of mortgage loans involve a third-party guarantee to be eligible for the exception. Ms. Seidman added that the loans had to be in the scope of Statement 65, which involves loans securitized by a mortgage banking enterprise with a substantial third-party guarantee. Ms. Donoghue responded that in practice, some have concluded that by analogy certain loans are similar enough to guaranteed mortgage loans that the guidance should apply to these loans as well.

12. Ms. Seidman stated that previously fair value for these loans had been considered transaction price so that valuing the loans to include servicing assets would have been appropriate. The issuance of FASB Statement No. 157, *Fair Value Measurements*, changed the definition of fair value, which is based on market price for the assets, not transaction price. Therefore, it would be more appropriate now to eliminate the exception to correlate the accounting with the updated definition of fair value.

Follow-up Items:

The Board will redeliberate the minimum threshold requirement for the amount of beneficial interests a third party must hold for a transferor to account for a transfer of financial assets as a sale.

General Announcements:

None.