

EITF ABSTRACTS

Issue No. 88-19

Title: FSLIC-Assisted Acquisitions of Thrifts

[Nullified by FAS 141(R)]

Dates Discussed: August 25-26, 1988; October 6, 1988; February 23, 1989

References: FASB Statement No. 72, *Accounting for Certain Acquisitions of Banking or Thrift Institutions*
FASB Statement No. 96, *Accounting for Income Taxes*
FASB Statement No. 109, *Accounting for Income Taxes*
FASB Statement No. 141, *Business Combinations*
FASB Statement No. 141 (revised 2007), *Business Combinations*
FASB Statement No. 142, *Goodwill and Other Intangible Assets*
FASB Statement No. 147, *Acquisitions of Certain Financial Institutions*
APB Opinion No. 16, *Business Combinations*
APB Opinion No. 17, *Intangible Assets*
SEC Staff Accounting Bulletin No. 82, *Certain Transfers of Nonperforming Assets*

ISSUE

A savings institution (Thrift) is acquired pursuant to an assistance agreement (Agreement) between the acquiror and the Federal Savings and Loan Insurance Corporation (FSLIC). Under the Agreement, the acquiror may receive a note receivable from the FSLIC, which typically equals the amount by which the fair value of the Thrift's liabilities exceeds the fair value of its assets. In addition, the acquiror may infuse additional capital into the Thrift that, with the FSLIC assistance, is expected to make the Thrift a viable entity.

The assistance provided by the FSLIC under the Agreement may include (1) yield maintenance assistance (which guarantees additional interest on specified interest-bearing assets, a level of return on specified non-interest-bearing assets, reimbursement if covered assets are ultimately collected or sold for amounts that are less than a specified amount, or any combination thereof), (2) indemnification against certain loss contingencies, and (3) the purchase by the FSLIC of

equity securities issued by the Thrift for cash or a note receivable from the FSLIC. Under the terms of the Agreement, the FSLIC may be entitled to share in certain tax benefits that may be realized subsequently by the Thrift.

The issues are:

1. How the acquiror should account for a tax-sharing arrangement with the FSLIC in which the FSLIC is entitled to share in a specified percentage (up to 100 percent) of certain income tax benefits that are realized by the Thrift
2. How the acquiror should account for assistance in the form of yield maintenance on covered assets until those assets are disposed of or liquidated
3. When allocating the purchase price, what interest rate should be used by the acquiror to determine the fair value of assets covered by yield maintenance assistance
4. Whether a change in basis should be recognized when an asset covered by yield maintenance assistance is converted into a different asset that continues to be covered by yield maintenance assistance
5. How the acquiror should account for contingency losses and for the reimbursement of those losses by the FSLIC under the indemnification provisions of the Agreement (including losses and reimbursements that occur after the expiration of the purchase price allocation period)
6. If part of the FSLIC assistance involves a note receivable from the FSLIC and equity securities of the Thrift are sold to the FSLIC for cash or other consideration, whether the Thrift should record an increase in equity for the issuance of those securities or offset the note receivable against that equity
7. If the note receivable from the FSLIC is offset against the equity from the securities issued to the FSLIC, how the Thrift should report subsequent interest payments received on the FSLIC note receivable and dividend payments made by the Thrift relating to those equity securities.

EITF DISCUSSION

Issue 1. The Task Force reached a consensus that the income tax benefits that the FSLIC is entitled to receive under the Agreement should be offset against the income tax benefits realized by the Thrift and the net tax benefit should be accounted for in accordance with generally accepted accounting principles (GAAP) for income taxes. This consensus is based on the view that the Thrift is merely a conduit for the tax benefits accruing to the FSLIC. [Note: This consensus has been nullified by Statement 141(R). See STATUS section.]

Issue 2. The Task Force reached a consensus that assets covered by yield maintenance assistance should be considered interest-bearing assets for purposes of applying Statement 72, even if the covered assets are non-interest bearing. Task Force members noted that the consensus applies only to regulatory-assisted combinations covered by Statement 72. [Note: This consensus has been nullified by Statement 141(R) and Statement 147. See Issue 2 in STATUS section.] They also agreed that a consequence of considering certain non-interest-bearing assets as interest-bearing assets is that those non-interest-bearing assets will affect the period over which goodwill is amortized in accordance with paragraph 5 of Statement 72. [Note: See Issue 2 in STATUS section.]

Issue 3. The Task Force reached a consensus that there is a rebuttable presumption that the stated interest rate (the guaranteed yield or level of return on covered assets) specified in the Agreement should be considered a market rate for purposes of determining the fair value of the assets acquired. If the presumption is rebutted, the acquiror should select a market rate in accordance with paragraph 88 of Opinion 16. [Note: This consensus has been nullified by Statement 141(R). See Issue 3 in STATUS section.]

Issue 4. The Task Force reached a consensus that no net change in the basis of the asset should be recognized if an asset covered by yield maintenance assistance is converted to a different covered asset (for example, land held for development is sold to an unrelated third party in exchange for a note receivable). [Note: This consensus has been nullified by Statement 141(R). See STATUS section.]

Issue 5. The Task Force reached a consensus that losses resulting from contingencies related to the acquisition that are covered by the indemnification provisions of the Agreement should be recognized by the acquiror net of reimbursements received or receivable from the FSLIC under the Agreement. [Note: This consensus has been nullified by Statement 141(R). See STATUS section.]

Issue 6. The Task Force reached a consensus that there is a rebuttable presumption that consideration paid by the FSLIC for equity securities is not separable from a note receivable from the FSLIC for other assistance. [Note: This consensus has been nullified by Statement 141(R). See STATUS section.] Therefore, when part of the FSLIC assistance involves a note receivable from the FSLIC, a portion of the note receivable equal to the fair value of the equity securities sold to the FSLIC should be offset against the equity securities. The Task Force noted that issuance of the equity securities to the FSLIC may be separately reported as an increase in equity only if it can be demonstrated that the equity security is economically separable from the note receivable from the FSLIC. The Task Force agreed that economic separability may be demonstrated only if all of the following conditions are met:

1. The regulator acquires equity securities for cash at the same per-share price as other shareholders, and the securities are identical in all substantive respects (except for voting rights) to those issued to other shareholders.
2. The portion of stock acquired by the regulator is less than 20 percent of the outstanding stock.
3. The dividend requirements on the stock held by the regulator are the same as on the stock held by others.
4. The dividend terms of the equity securities do not match and offset the principal and interest terms of the note receivable.
5. Repayment of principal and interest on the note is due independently of dividend or redemption payments.
6. The interest rate stated in the note receivable from the regulator is a market rate.
7. The stock cannot be put back to the institution by the regulator (however, callable stock is acceptable).

Issue 7. The Task Force reached a consensus that if all or a portion of the note receivable from the FSLIC is offset against the equity from the securities issued to the FSLIC, then subsequent dividend payments to the FSLIC on the equity securities should be netted against cash receipts from the FSLIC for interest payments on the note, and the net amount should be recorded as regulatory assistance, as appropriate. [Note: This consensus has been nullified by Statement 141(R). See STATUS section.]

The Task Force noted that the above consensuses apply to all regulatory-assisted acquisitions of banking and thrift institutions.

The SEC Observer stated that he would expect publicly held companies to disclose as separate line items in the balance sheet and income statement the effect of the FSLIC or other regulatory assistance regardless of its form and manner of calculation. Thus, users of those statements should be able to assess the ongoing financial condition and operations of the acquired entity as if that assistance did not exist. The SEC Observer added that full disclosure of the nature, amounts, and terms of all forms of regulatory assistance is required by the SEC's full disclosure requirements as well as by paragraph 11 of Statement 72. [Note: See Issue 2 in STATUS section.]

The Task Force reviewed two examples, which are presented in Exhibit 88-19A, that illustrate the application of the consensuses and the SEC staff's requirements regarding financial statement presentation. Example 1 illustrates the application of the Task Force consensuses on Issues 1 through 5 and identifies an alternative method of income statement presentation. The SEC Observer stated that either alternative identified in the exhibit is acceptable to the SEC staff. Example 2 illustrates the application of the Task Force consensuses on Issues 6 and 7.

A Task Force member questioned whether application of the SEC staff's display requirements would require an entity, subsequent to the acquisition date, to adjust the balance sheet amounts of the underlying asset and the FSLIC assistance if the value of the underlying asset had increased above its cost basis. For example, if the value of the raw land in Example 1 of Exhibit 88-19A had increased from its \$50 fair value at the acquisition date to \$60 at the end of year 1, should the balance sheet at the end of year 1 reflect raw land of \$60 and FSLIC assistance related to that land of \$20? This question was asked in the context of balance sheet display only.

In response to this question, the SEC Observer indicated that the SEC staff would not insist that such adjustments be reflected in the balance sheet because to do so would be to reflect the

underlying asset, raw land, at an amount different from that appropriate under GAAP. However, disclosure of such changes in value may be appropriate. The SEC Observer emphasized that the SEC staff's display requirements would require an adjustment to the carrying amount of the underlying asset only if such adjustment is required under GAAP (for example, for impairment in the value of the underlying asset).

STATUS

Since the discussion of this Issue, the SEC staff has worked with individual registrants who have effected FSLIC-assisted acquisitions of financial institutions. The SEC staff has determined that it will not object to an alternative method of displaying the impact of regulatory assistance provided that method meets the staff's overall objective. An acceptable alternative approach includes prominent display of assets covered by FSLIC assistance as one line item on the face of the balance sheet and appropriate segregation in the income statement of the effect of FSLIC assistance. A referenced footnote should present, among other things, a breakdown of the major categories of covered assets and the income derived therefrom, the estimated fair value of underlying assets, and the estimated amount of the FSLIC receivable at each reporting date.

On July 5, 1989, the SEC staff issued SAB 82, which discusses accounting for transfers of nonperforming assets by financial institutions and disclosure of the impact of financial assistance from regulators. SAB 82 states the SEC staff's belief that users of financial statements must be able to assess the impact of credit and other risks on a company following a regulatory-assisted acquisition, transfer, or other reorganization on a basis comparable to that disclosed by other institutions, that is, as if the assistance did not exist. In that regard, the SEC staff believes that the amount of regulatory assistance should be disclosed separately and should be separately identified in the statistical information furnished pursuant to SEC Industry Guide 3, to the extent it impacts such information. Further, the nature, extent, and impact of such assistance should be fully disclosed in Management's Discussion and Analysis.

Since the date of the consensus, the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA) dissolved the FSLIC; however, the consensus still applies to regulatory-assisted acquisitions.

In February 1992, the FASB issued Statement 109, which supersedes Statement 96 and affects the accounting for business combinations.

Statement 109 requires that a deferred tax liability or asset be recognized for the estimated future tax effects attributable to temporary differences and carryforwards. Paragraph 17 of Statement 109 requires measurement of a deferred tax asset for deductible temporary differences and operating loss carryforwards using the applicable tax rate. Deferred tax assets are reduced by a valuation allowance if, based on the weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

Paragraph 30 provides guidance on business combinations and states that if a valuation allowance is recognized for the deferred tax asset for an acquired entity's deductible temporary differences or operating loss or tax credit carryforwards at the acquisition date, the tax benefits for those items that are first recognized (that is, by elimination of the valuation allowance) in financial statements after the acquisition date shall be applied (a) first to reduce to zero any goodwill related to the acquisition, (b) second to reduce to zero other noncurrent intangible assets related to the acquisition, and (c) third to reduce income tax expense.

Additional amounts of deductible temporary differences and operating loss or tax credit carryforwards may arise after the acquisition date and before recognition of the tax benefit of amounts existing at the acquisition date. The tax benefit of amounts arising after the acquisition date is recognized as a reduction of income tax expense. Whether a tax benefit recognized in later years is attributable to an amount existing at or arising after the acquisition date is determined for financial reporting by provisions in the tax law that identify the sequence in which those amounts are utilized for tax purposes. If not determinable by provisions in the tax

Copyright © 2008, Financial Accounting Standards Board

Not for redistribution

law, a tax benefit recognized for financial reporting is prorated between a reduction of (a) goodwill and other noncurrent intangible assets and (b) income tax expense.

Issue 2. Statement 147 was issued in October 2002 and supersedes paragraphs 8–11 of Statement 72 that provided guidance on accounting for regulatory-assisted combinations. Statement 147 also amends Statement 72 to remove all financial institution acquisitions (except for transactions between mutual enterprises) from the scope of Statement 72. Statement 147 requires acquisitions of financial institutions (except for those between mutual enterprises) to be accounted for in accordance with Statements 141 and 142. Statement 141(R), which was issued in December 2007, nullifies Statement 147 and this Issue. However, this Issue still applies to mergers and acquisitions by not-for-profit organizations, which will be further considered as part of a separate FASB project that was exposed for comment in proposed Statements, *Not-for-Profit Organizations: Mergers and Acquisitions*, and *Not-for-Profit Organizations: Goodwill and Other Intangible Assets Acquired in a Merger or Acquisition*. Statement 141(R) is effective for business combinations with an acquisition date on or after the beginning of the first annual reporting period beginning on or after 12/15/08.

Issue 3. Statement 141, which superseded Opinion 16, was issued in June 2001. The market rate guidance for assets acquired provided in paragraph 88 of Opinion 16 was carried forward without reconsideration in paragraph 37 of Statement 141. Statement 141(R) replaces Statement 141 and supersedes Opinion 16 and nullifies this Issue. However, this Issue still applies to mergers and acquisitions by not-for-profit organizations, which will be further considered as part of a separate FASB project. Statement 141(R) is effective for business combinations with an acquisition date on or after the beginning of the first annual reporting period beginning on or after 12/15/08.

No further EITF discussion is planned.

Exhibit 88-19A

**EXAMPLES OF THE APPLICATION OF THE EITF CONSENSUSES ON ISSUE 88-19
AND THE SEC'S REQUIREMENTS REGARDING FINANCIAL STATEMENT
PRESENTATION OF AN FSLIC-ASSISTED ACQUISITION OF A THRIFT**

Example 1 [Note: See Issue 2 in STATUS section.]

Description of Transaction

An acquiror infuses \$10 cash into a troubled Thrift and assumes the Thrift's net liabilities in exchange for 100 percent of the common stock. The historical cost balance sheet of the Thrift at date of acquisition was as follows:

<u>Assets</u>		<u>Liabilities and Deficit</u>	
Loans	\$100	Deposits	\$250
Raw land	<u>80</u>	Deficit	<u>(70)</u>
Total assets	<u>\$180</u>	Total liabilities and deficit	<u>\$180</u>

In connection with the acquisition, the FSLIC agrees to provide the following forms of assistance:

1. The FSLIC will issue a note with a face amount of \$60 at 10 percent.
2. The FSLIC will guarantee a 10 percent yield on the original book value of the raw land (\$80) and will guarantee the recovery of \$80 when sold.
3. The FSLIC will guarantee the recovery of one loan at its carrying value on the books of the Thrift (\$50) and a 10 percent yield on that loan. This guarantee continues in force if the loan is foreclosed or otherwise converted to another asset.
4. The FSLIC will receive 50 percent of any tax benefits realized by the Thrift on its tax return, both those arising from net operating losses (NOLs) existing at the acquisition date and those arising from NOLs incurred subsequent to that date.
5. The FSLIC will indemnify the acquiror against loss contingencies arising after the acquisition date.

Assumptions:

1. There is no evidence to overcome the rebuttable presumption that the stated rate on the FSLIC note and the yield maintenance is considered to be a market rate, as discussed in the Task Force consensus on Issue 3, and therefore 10 percent is determined to be a market rate.

2. The fair value of the raw land is \$50.
3. The loans and deposits have a stated rate of 10 percent.
4. The fair values of the loans, other than the covered loan, and the deposits are equal to book value. The fair value of the covered loan is \$40.
5. There is a preexisting NOL of \$15; the NOL cannot be utilized to offset other taxable income of the acquiror. Statement 96 has been adopted. There are no temporary differences either existing at the date of acquisition or arising subsequently. The effective tax rate is 33 percent. [Note: See STATUS section.]
6. Interest income on the FSLIC note, as well as payments received from the FSLIC relating to yield maintenance, capital maintenance, and indemnification of losses, are not taxable to the Thrift.
7. Solely for purposes of simplifying this example, no core deposits or other specific intangibles are identified.
8. No principal reductions on the loan, deposits, or the FSLIC note are assumed.

New Basis Balance Sheet as of the Acquisition Date

<u>Assets</u>		<u>Liabilities and Equity</u>	
Cash	\$ 10	Deposits	\$250
Loans:			
Covered loans ^a	\$40		
FSLIC assistance ^a	10		
Other loans	<u>50</u>		
Total	100		
FSLIC note receivable ^a	60		
Other covered assets: ^a			
Raw land	50		
FSLIC assistance	<u>30</u>		
Total	80	Equity	<u>10</u>
Goodwill ^b	<u>10</u>		
Total assets	<u>\$260</u>	Total liabilities and equity	<u>\$260</u>

^aDisclosure of the nature of the FSLIC assistance and the note receivable from the FSLIC should be made in a footnote.

^bThe goodwill should be amortized in accordance with Statement 72 over the estimated remaining life of the long-term, interest-bearing assets acquired, including the note receivable from the FSLIC and, pursuant to the Task Force consensus related to the second issue, the covered assets. Solely for purposes of simplifying this example, goodwill is assumed to be amortized on a straight-line basis over 10 years. [Note: See Issue 2 in STATUS section.]

Transactions—Year 1

Due to a deterioration in the credit quality subsequent to the acquisition date, the covered loan is foreclosed and real estate is received that has a fair value of \$30. For ease of computation, it is assumed that the foreclosure occurred on the last day of the year and that interest for the entire year at the 10 percent contractual rate had been received from the borrower and appropriately recognized.

	<u>Debit</u>	<u>Credit</u>
<u>Journal Entries</u>		
Provision for loan losses	10	
Allowance for loan losses		10
Real estate acquired in foreclosure	30	
Allowance for loan losses	10	
Loans receivable		40
Other covered assets—FSLIC receivable	10	
Other income—effect of FSLIC assistance		10
To record loan loss, foreclosure, and impact of the FSLIC indemnification of loan loss		
Other covered assets—FSLIC receivable	10	
Covered loans—FSLIC receivable		10
To reclassify the FSLIC assistance on covered loan to asset category to which it now relates		

A loss contingency relating to litigation arises subsequent to the acquisition date, resulting in a settlement of \$5, which is reimbursed by the FSLIC.

	<u>Debit</u>	<u>Credit</u>
<u>Journal Entries</u>		
Other expense	5	
Cash		5
Cash	5	
Other income—effect of FSLIC assistance		5

The FSLIC makes the yield maintenance payment relating to the land of \$8 ($\$80 \times 10\%$), and it is credited to income in accordance with paragraph 8 of Statement 72.

Journal Entry

Cash	8	
Other income—effect of FSLIC assistance		8

Income Statement—Year 1

Interest income:

Loans ($\$100 \times 10\%$)	\$10
FSLIC note receivable ($\$60 \times 10\%$)	<u>6^a</u>
Total	16

Interest expense:

Deposits ($\$250 \times 10\%$)	<u>25</u>
Net interest income (expense)	(9)

Provision for loan loss	<u>10</u>
Net interest income (expense) after provision	(19)

Other income:

Effect of FSLIC assistance	23 ^b
----------------------------	-----------------

Other expenses:

Litigation settlement	5
Amortization of goodwill	<u>1</u>
Total	6

^aAlternatively, interest income relating to the FSLIC note receivable may be included in the caption *Other income—effect of FSLIC assistance*.

^bThe following detail of the FSLIC assistance would be presented in a footnote:

Yield maintenance on covered assets	\$ 8
Capital loss coverage	10
Loss contingency indemnification	<u>5</u>
Total	<u>\$23</u>

Loss before income taxes	(2)
Income tax expense	<u>0^c</u>
Net loss	<u>\$(2)</u>

Transactions—Year 2

Due to the sale at year-end of the remaining loans for a \$65 gain, net taxable income of \$45 is earned. The Thrift realizes the tax benefit associated with the preexisting NOL of \$15, as well as the NOL generated in year 1 of \$30. At a 33 percent tax rate, the resulting tax benefit is \$15. Of this, \$7.50 (50 percent) must be shared with the FSLIC.

	<u>Debit</u>	<u>Credit</u>
<u>Journal Entries</u>		
Income tax expense	15	
Current taxes payable		15
To recognize effects of current year taxable income ($\$45 \times 33\%$)		
Current taxes payable	15	
Goodwill ($\$15 \times 33\%$)		5
Income tax expense ($\$30 \times 33\%$)		10
To recognize effects of NOL carryforward		

^cThe NOL carryforward is computed as follows (assume no preexisting or arising timing or temporary differences):

Taxable income:	
Interest	\$10
Tax deductions:	
Interest on deposits	25
Provision for loan loss (realized)	10
Litigation settlement	<u>5</u>
Total	<u>40</u>
Tax loss—year 1	30
NOL carryforward at acquisition	<u>15</u>
Total NOL carryforward	<u>\$45</u>

	<u>Debit</u>	<u>Credit</u>
Other income—effect of FSLIC assistance	5	
Goodwill	2.50	
Payable to FSLIC		7.50
To recognize effects of NOL sharing arrangement with FSLIC		

The FSLIC makes the yield maintenance payment of \$13, reflecting a 10 percent yield on \$130 (the raw land of \$80 and the real estate foreclosed in year 1 of \$50). The payment is credited to income in accordance with paragraph 8 of Statement 72.

Journal Entry

Cash	13	
Other income—effect of FSLIC assistance		13

Income Statement—Year 2

Interest income:

Loans ($\$50 \times 10\%$)	\$ 5
FSLIC note receivable ($\$60 \times 10\%$)	<u>6</u>
Total	11

Interest expense:

Deposits ($\$250 \times 10\%$)	<u>25</u>
Net interest income (expense)	(14)

Provision for loan loss	<u>0</u>
Net interest income (expense) after provision	(14)

Other income:

Gain on sale of loans	65
Effect of FSLIC assistance	<u>8^a</u>
Total	73

^aThe following detail of the FSLIC assistance would be presented in a footnote:

Yield maintenance	\$13
FSLIC share of NOL benefit	<u>(5)</u>
Total	<u>\$ 8</u>

Other expense:	
Amortization of goodwill	<u>1</u>
Income before income taxes	58
Income tax expense	<u>5^b</u>
Net income	<u>\$53</u>

Alternative Income Statement Presentation

An alternative to the foregoing income statement presentation follows. Rather than presenting the FSLIC assistance as one line item in the *Other income* category of the income statement, separate line item disclosure of each component in the portion of the income statement to which it relates would be presented.

For example, in the previous example for year 1, the following components of FSLIC assistance were identified:

Yield maintenance on covered assets	\$ 8
Capital loss coverage	10
Loss contingency indemnification	<u>5</u>
Total	<u>\$23</u>

Under the alternative approach, each of those items would be presented separately as an offset to the income or expense item to which it relates: (1) *FSLIC yield maintenance on covered assets* would be a separate line item within interest income, (2) *FSLIC capital loss coverage* would be a separate line item within the provision for loan losses, and (3) *FSLIC loss contingency indemnification* would be a separate line item within other expenses.

^bComputation of taxable income before utilization of NOL (see previous page for computation of tax expense):

Interest income	\$ 5
Gain on sale of loans	<u>65</u>
Total	70
Interest expense	<u>25</u>
Taxable income	<u>\$45</u>

Under the alternative approach for year 2, (1) *FSLIC yield maintenance on covered assets* would be a separate line item within interest income, and (2) *FSLIC share of NOL benefit* would be a separate line item within income tax expense.

Example 2

Description of Transaction

Assume the same facts as Example 1, except that the Thrift issues preferred stock with a value of \$5 to the FSLIC, and the FSLIC infuses cash of \$5. Economic separability cannot be demonstrated because all of the conditions specified in the consensus on Issue 6 have not been met. Dividends are paid on the equity security at 10 percent.

New Basis Balance Sheet as of the Acquisition Date

<u>Assets</u>		<u>Liabilities and Equity</u>	
Cash	\$ 15	Deposits	\$250
Loans:			
Covered loans ^a	\$40		
FSLIC assistance ^a	10		
Other loans	<u>50</u>		
Total	100		
FSLIC note receivable ^a	55		
Other covered assets: ^a			
Raw land	50		
FSLIC assistance	<u>30</u>		
Total	80	Equity:	
Goodwill	<u>10</u>	Preferred	0 ^b
		Common	<u>10</u>
		Total liabilities	
Total assets	<u>\$260</u>	and equity	<u>\$260</u>

^aDisclosure of the nature of the FSLIC assistance and the note receivable from the FSLIC should be made in a footnote.

^bDisclosure of the composition of this account should be made either on the face of the balance sheet or in a footnote. For example, preferred stock with a value of \$5 has been offset by a portion of the note receivable from the FSLIC (\$5) received in connection with the assistance agreement.

Transactions—Year 1

The Thrift pays dividends of \$.50 ($\$5 \times 10\%$) on the preferred stock. The FSLIC pays interest on the note of \$6 ($\$60 \times 10\%$).

	<u>Debit</u>	<u>Credit</u>
<u>Journal Entries</u>		
Cash	6	
Interest income—FSLIC note		6
Retained earnings (preferred dividend)	.50	
Cash		.50
Interest income—FSLIC note	.50	
Retained earnings (preferred dividend)		.50