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***Proposed Amendment to SFAS 140: Board Chooses to Redeliberate
Additional Issues***

Introduction

On June 7th, 2006, the Financial Accounting Standards Board (“FASB” or “Board”) decided to proceed with, and redeliberate certain issues related to, the SFAS 140 transfer project as proposed in the October 10th, 2005 Exposure Draft (revised) of the Proposed SFAS, *Accounting for Transfers of Financial Assets, an amendment of FASB Statement No. 140*, a revision of the ED issued on June 10th, 2003. At the June meeting, the Board reached decisions whether to redeliberate, reaffirm previous decisions or drop from consideration a number of issues identified from the comment letter process.

At its July 26th meeting, the Board continued to discuss certain open issues related to the project, including:

- Rollovers of beneficial interests;
- Participating interests (paragraph 8(a)); and
- Transferability requirements (paragraph 9(b)).

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Rollovers of Beneficial Interests

The FASB staff recommended and the Board agreed, to redeliberate the proposed guidance on rollovers of beneficial interests and to determine whether to:

1. Disallow rollovers.
2. Clarify the meaning of “more-than-trivial incremental benefit.”
3. Provide examples of acceptable and unacceptable combinations of involvements by a single party.
4. Clarify the guidance for beneficial interests issued by a master trust.
5. Consider other alternatives.

SFG Observation: *The ED’s proposed amendments to SFAS 140 relate to QSPEs that reissue or “roll over” beneficial interests. Specifically, it defined “reissuance of beneficial interests”, clarified that issuances from master trusts would not be considered the reissuance of beneficial interests, and concluded that an SPE would not be qualifying if any party to the transaction had more than one involvement with the entity and was able to obtain a “more-than-trivial incremental benefit” by virtue of the combination of those involvements.*

Numerous comment letters objected to the ED’s proposed guidance. Some considered the concept unoperational (how is a “more-than-trivial incremental benefit” to be assessed?); others asserted that a “benefit”-based test is inconsistent with the control-based approach that undergirds the SFAS 140 model.

Permitted Activities of a QSPE

In December 2005, the Board added to its agenda a project to provide interpretive guidance regarding the permitted activities (and related discretion) that a servicer can exercise on behalf of a QSPE. Evaluating whether (or to what extent) a QSPE may rollover beneficial interests and whether a QSPE’s servicer may permissibly engage in certain servicing activities must be considered in light of paragraph 35(b) of SFAS 140, which directs that the activities of a QSPE be “significantly limited” and “entirely specified”. The FASB staff recommended that the Board addresses these issues pertaining to the permitted activities of QSPE jointly for efficiency and to ensure that consistent guidance is provided for those related issues.

The Board agreed to combine the servicer discretion project into the transfers project and deliberate all matters related to the permitted activities and investments of a QSPE under this one project.

The FASB staff identified the following issues relating to permitted activities and permissible investments that they expect to address in this combined part of the project:

- Rollovers of beneficial interests;
- Equity investments in a QSPE;
- Limitations on derivatives in a QSPE; and
- Servicer discretion in;
 - a) waiving a due-on-sale provision;
 - b) substituting collateral with respect to a loan held by a QSPE; and
 - c) connection with the potential foreclosure and sale of related estate temporarily held by a QSPE

Derivatives held by a QSPE

An earlier decision by the Board in the transfers project would have eliminated the present restriction in SFAS 140 that proscribes a QSPE from holding passive derivative financial instruments deemed to “pertain to” beneficial interests held by the transferor. The revised ED incorporated this change – one of the few provisions in the proposal endorsed by virtually all constituents who commented.

At the June 7th meeting, the Board decided to delete this change from the proposed statement – thus leaving the present restriction intact. However, after receiving a number of comment letters expressing concern over this decision, the FASB staff recommended and the Board agreed to continue discussions on the use of derivatives in QSPEs.

SFG Observation: *The Board devoted little time to deliberating this matter at the June 7th meeting before agreeing to delete the proposed relief -- an outcome that caught many observers by surprise. The decision to reconsider that action is a welcome one.*

Participating interests and transferability requirements

These two issues relate to transfers of assets (or transfers of interests in those assets) that involve multiple steps and/or a QSPE as the ultimate transferee, and related issues of derecognition. The current ED prescribes conditions more stringent than current practice for a transferor to achieve sales accounting. The FASB staff recommended that the Board defers making a decision about whether to retain these new de-recognition requirements in the final standard until the Board has completed its redeliberations regarding (1)

permitted activities of a QSPE and (2) the effects of a transferor's continuing involvement with a transferred asset relative to the isolation evaluation. The Board will make a decision regarding the participating interests and transferability requirements after these deliberations have been completed.

SFG Observation: *In its deliberations leading up to the new ED, the Board devoted significant time to discussing under what circumstances de-recognition is appropriate for transfers involving participating (undivided) interests in financial assets. Currently, transfers of such interests may qualify for derecognition, although no QSPE is involved. The ED provides a new definition and guidance for transfers of participating interests significantly more restrictive than current practice.*

Next step

The FASB staff indicated that they expect to report back to the Board in September on the results of their research relating to a QSPE's permitted activities/investments and to make related recommendations for the Board's consideration.

Questions

Questions regarding this advisory may be directed to:

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