Statement of Financial Accounting Standards No. 107

FAS107 Status Page
FAS107 Summary

Disclosures about Fair Value of Financial Instruments

December 1991

Financial Accounting Standards Board
of the Financial Accounting Foundation
401 MERRITT 7, P.O. BOX 5116, NORWALK, CONNECTICUT 06856-5116

Copyright © 1991 by Financial Accounting Standards Board. All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted, in any form or by any means, electronic, mechanical, photocopying, recording, or otherwise, without the prior written permission of the Financial Accounting Standards Board.

Statement of Financial Accounting Standards No. 107

Disclosures about Fair Value of Financial Instruments

December 1991

CONTENTS

Paragraph Numbers

Introduction 1–2
Standards of Financial Accounting and Reporting:
Definitions and Scope 3–9
Disclosures about Fair Value of Financial Instruments 10–15
Effective Dates and Transition 16–17
Appendix A: Examples of Procedures for Estimating Fair Value 18–29
Appendix B: Illustrations Applying the Disclosure Requirements about Fair Value of Financial Instruments 30–33
Appendix C: Background Information and Basis for Conclusions 34–88

FAS 107: Disclosures about Fair Value of Financial Instruments

FAS 107 Summary

This Statement extends existing fair value disclosure practices for some instruments by requiring all entities to disclose the fair value of financial instruments, both assets and liabilities recognized and not recognized in the statement of financial position, for which it is practicable to estimate fair value. If estimating fair value is not practicable, this Statement requires disclosure of descriptive information pertinent to estimating the value of a financial instrument. Disclosures about fair value are not required for certain financial instruments listed in paragraph 8.

This Statement is effective for financial statements issued for fiscal years ending after December 15, 1992, except for entities with less than $150 million in total assets in the current statement of financial position. For those entities, the effective date is for fiscal years ending after December 15, 1995.

INTRODUCTION

1. The FASB added a project on financial instruments and off-balance-sheet financing to its agenda in May 1986. The project is expected to develop broad standards to aid in resolving existing financial accounting and reporting issues and other issues likely to arise in the future about various financial instruments and related transactions.

2. Because of the complexity of the issues about how financial instruments and transactions should be recognized and measured, the Board decided that, initially, improved disclosure of information about financial instruments is necessary. The first disclosure phase was completed in March 1990 with the issuance of FASB Statement No. 105, *Disclosure of Information about Financial Instruments with Off-Balance-Sheet Risk and Financial Instruments with Concentrations of Credit Risk.* The second phase, which resulted in this Statement, considers disclosures about fair value of all financial instruments, both assets and liabilities recognized and not recognized in the statement of financial position, except those listed in paragraph 8.

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

Definitions and Scope

3. A financial instrument is defined as cash, evidence of an ownership interest in an entity, or a contract that both:

a. Imposes on one entity a contractual obligation [1] (1) to deliver cash or another financial instrument [2] to a second entity or (2) to exchange other financial instruments on potentially unfavorable terms with the second entity
b. Conveys to that second entity a contractual right [3] (1) to receive cash or another financial instrument from the first entity or (2) to exchange other financial instruments on potentially favorable terms with the first entity.

4. The definition in paragraph 3 is essentially the same as that in paragraph 6 of Statement 105, which is hereby amended to conform to this Statement. Appendix A of Statement 105 provides examples of instruments that are included in and excluded from the definition of a financial instrument.

5. For purposes of this Statement, the fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. If a quoted market price is available for an instrument, the fair value to be disclosed for that instrument is the product of the number of trading units of the instrument times that market price.

6. Under the definition of fair value in paragraph 5, the quoted price for a single trading unit in the most active market is the basis for determining market price and reporting fair value. This is the case even if placing orders to sell all of an entity's holdings of an asset or to buy back all of a liability might affect the price, or if a market's normal volume for one day might not be sufficient to absorb the quantity held or owed by an entity.

7. This Statement requires disclosures about fair value for all financial instruments, whether recognized or not recognized in the statement of financial position, except for those specifically listed in paragraph 8. It applies to all entities. It does not change any requirements for recognition, measurement, or classification of financial instruments in financial statements.

8. The disclosures about fair value prescribed in paragraphs 10-14 are not required for the following:

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

a. Employers' and plans' obligations for pension benefits, other postretirement benefits including health care and life insurance benefits, employee stock option and stock purchase plans, and other forms of deferred compensation arrangements, as defined in FASB Statements No. 35, *Accounting and Reporting by Defined Benefit Pension Plans,* No. 87, *Employers' Accounting for Pensions,* No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions,* and No. 43, *Accounting for Compensated Absences,* and APB Opinions No. 25, *Accounting for Stock Issued to Employees,* and No. 12, *Omnibus Opinion—1967*
b. Substantively extinguished debt subject to the disclosure requirements of FASB Statement No. 76, *Extinguishment of Debt,* and assets held in trust in connection with an in-substance defeasance of that debt
c. Insurance contracts, other than financial guarantees and investment contracts, as discussed in FASB Statements No. 60, *Accounting and Reporting by Insurance Enterprises,* and No. 97, *Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments*
d. Lease contracts as defined in FASB Statement No. 13, *Accounting for Leases* (a contingent obligation arising out of a cancelled lease and a guarantee of a third-party lease obligation are not lease contracts and are included in the scope of this Statement)
e. Warranty obligations and rights
f. Unconditional purchase obligations as defined in paragraph 6 of FASB Statement No. 47, *Disclosure of Long-Term Obligations*
g. Investments accounted for under the equity method in accordance with the requirements of APB Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock*
h. Minority interests in consolidated subsidiaries
i. Equity investments in consolidated subsidiaries
j. Equity instruments issued by the entity and classified in stockholders' equity in the statement of financial position.

9. Generally accepted accounting principles already require disclosure of or subsequent measurement at fair value for many classes of financial instruments. Although the definitions or the methods of estimation of fair value vary to some extent, and various terms such as market value, current value, or mark-to-market are used, the amounts computed under those requirements satisfy the requirements of this Statement and those requirements are not superseded or modified by this Statement.

Disclosures about Fair Value of Financial Instruments

10. An entity shall disclose, either in the body of the financial statements or in the accompanying notes, the fair value of financial instruments for which it is practicable to estimate that value. An entity also shall disclose the method(s) and significant assumptions used to estimate the fair value of financial instruments.

11. Quoted market prices, if available, are the best evidence of the fair value of financial

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

instruments. If quoted market prices are not available, management's best estimate of fair value may be based on the quoted market price of a financial instrument with similar characteristics or on valuation techniques (for example, the present value of estimated future cash flows using a discount rate commensurate with the risks involved, option pricing models, or matrix pricing models). Appendix A of this Statement contains examples of procedures for estimating fair value.

12. In estimating the fair value of deposit liabilities, a financial entity shall not take into account the value of its long-term relationships with depositors, commonly known as core deposit intangibles, which are separate intangible assets, not financial instruments. For deposit liabilities with no defined maturities, the fair value to be disclosed under this Statement is the amount payable on demand at the reporting date. This Statement does not prohibit an entity from disclosing separately the estimated fair value of any of its nonfinancial intangible and tangible assets and nonfinancial liabilities.

13. For trade receivables and payables, no disclosure is required under this Statement when the carrying amount approximates fair value.

14. If it is not practicable for an entity to estimate the fair value of a financial instrument or a class of financial instruments, the following shall be disclosed:

a. Information pertinent to estimating the fair value of that financial instrument or class of financial instruments, such as the carrying amount, effective interest rate, and maturity
b. The reasons why it is not practicable to estimate fair value.

15. In the context of this Statement, *practicable* means that an estimate of fair value can be made without incurring excessive costs. It is a dynamic concept: what is practicable for one entity might not be for another; what is not practicable in one year might be in another. For example, it might not be practicable for an entity to estimate the fair value of a class of financial instruments for which a quoted market price is not available because it has not yet obtained or developed the valuation model necessary to make the estimate, and the cost of obtaining an independent valuation appears excessive considering the materiality of the instruments to the entity. Practicability, that is, cost considerations, also may affect the required precision of the estimate; for example, while in many cases it might seem impracticable to estimate fair value on an individual instrument basis, it may be practicable for a class of financial instruments in a portfolio or on a portfolio basis. In those cases, the fair value of that class or of the portfolio should be disclosed. Finally, it might be practicable for an entity to estimate the fair value only of a subset of a class of financial instruments; the fair value of that subset should be disclosed.

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

Effective Dates and Transition

16. This Statement shall be effective for financial statements issued for fiscal years ending after December 15, 1992, except for entities with less than $150 million in total assets in the current statement of financial position. For those entities, the effective date shall be for financial statements issued for fiscal years ending after December 15, 1995. Earlier application is encouraged. In the initial year of application of this Statement, it need not be applied to complete interim financial statements.

17. Disclosures required by paragraphs 10-14 that have not previously been reported need not be included in financial statements that are being presented for comparative purposes for fiscal years ending before the applicable effective date of this Statement for an entity. For all subsequent fiscal years, the information required to be disclosed by this Statement shall be included for each year for which a statement of financial position is presented for comparative purposes.

The provisions of this Statement need not be applied to immaterial items.

This Statement was adopted by the unanimous vote of the six members of the Financial Accounting Standards Board:

Dennis R. Beresford, *Chairman*
Joseph V. Anania
Victor H. Brown
James J. Leisenring
A. Clarence Sampson
Robert J. Swieringa

Appendix A: EXAMPLES OF PROCEDURES FOR ESTIMATING FAIR VALUE

18. This appendix provides examples of procedures for estimating the fair value of financial instruments. The examples are illustrative and are not meant to portray all possible ways of estimating the fair value of a financial instrument in order to comply with the provisions of this Statement.

19. Fair value information is frequently based on information obtained from market sources. In broad terms, there are four kinds of markets in which financial instruments can be bought,

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

sold, or originated; available information about prices differs by kind of market:

a. *Exchange market.* An exchange or "auction" market provides high visibility and order to the trading of financial instruments. Typically, closing prices and volume levels are readily available in an exchange market.
b. *Dealer market.* In a dealer market, dealers stand ready to trade—either buy or sell—for their own account, thereby providing liquidity to the market. Typically, current bid and asked prices are more readily available than information about closing prices and volume levels. "Over-the-counter" markets are dealer markets.
c. *Brokered market.* In a brokered market, brokers attempt to match buyers with sellers but do not stand ready to trade for their own account. The broker knows the prices bid and asked by the respective parties, but each party is typically unaware of another party's price requirements; prices of completed transactions are sometimes available.
d. *Principal-to-principal market.* Principal-to-principal transactions, both originations and resales, are negotiated independently, with no intermediary, and little, if any, information is typically released publicly.

Financial Instruments with Quoted Prices

20. As indicated in paragraph 11 of this Statement, quoted market prices, if available, are the best evidence of fair value of financial instruments. Prices for financial instruments may be quoted in several markets; generally, the price in the most active market will be the best indicator of fair value.

21. In some cases, an entity's management may decide to provide further information about the fair value of a financial instrument. For example, an entity may want to explain that although the fair value of its long-term debt is less than the carrying amount, settlement at the reported fair value may not be possible or may not be a prudent management decision for other reasons; or the entity may want to state that potential taxes and other expenses that would be incurred in an actual sale or settlement are not taken into consideration.

Financial Instruments with No Quoted Prices

22. For financial instruments that do not trade regularly, or that trade only in principal-to-principal markets, an entity should provide its best estimate of fair value. Judgments about the methods and assumptions to be used in various circumstances must be made by those who prepare and attest to an entity's financial statements. The following discussion provides some examples of how fair value might be estimated.

23. For some short-term financial instruments, the carrying amount in the financial statements may approximate fair value because of the relatively short period of time between the origination of the instruments and their expected realization. Likewise, for loans that reprice frequently at market rates, the carrying amount may normally be close enough to fair value to satisfy these

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

disclosure requirements, provided there is no significant change in the credit risk of those loans.

24. Some financial instruments (for example, interest rate swaps and foreign currency contracts) may be "custom-tailored" and, thus, may not have a quoted market price. In those cases, an estimate of fair value might be based on the quoted market price of a similar financial instrument, adjusted as appropriate for the effects of the tailoring. Alternatively, the estimate might be based on the estimated current replacement cost of that instrument.

25. Other financial instruments that are commonly "custom-tailored" include various types of options (for example, put and call options on stock, foreign currency, or interest rate contracts). A variety of option pricing models that have been developed in recent years (such as the Black-Scholes model and binomial models) are regularly used to value options. The use of those pricing models to estimate fair value is appropriate under the requirements of this Statement.

26. For some predominantly financial entities, loans receivable may be the most significant category of financial instruments. Market prices may be more readily available for some categories of loans (such as residential mortgage loans) than for others. If no quoted market price exists for a category of loans, an estimate of fair value may be based on (a) the market prices of similar traded loans with similar credit ratings, interest rates, and maturity dates, (b) current prices (interest rates) offered for similar loans in the entity's own lending activities, or (c) valuations obtained from loan pricing services offered by various specialist firms or from other sources.

27. An estimate of the fair value of a loan or group of loans may be based on the discounted value of the future cash flows expected to be received from the loan or group of loans. The selection of an appropriate current discount rate reflecting the relative risks involved requires judgment, and several alternative rates and approaches are available to an entity. A single discount rate could be used to estimate the fair value of a homogeneous category of loans; for example, an entity might apply a single rate to each aggregated category of loans reported for regulatory purposes. An entity could use a discount rate commensurate with the credit, interest rate, and prepayment risks involved, which could be the rate at which the same loans would be made under current conditions. An entity also could select a discount rate that reflects the effects of interest rate changes and then make adjustments to reflect the effects of changes in credit risk. Those adjustments could include (a) revising cash flow estimates for cash flows not expected to be collected, (b) revising the discount rate to reflect any additional credit risk associated with that group of loans, or some combination of (a) and (b).

28. A fair value for financial liabilities for which quoted market prices are not available can generally be estimated using the same techniques used for estimating the value of financial assets. For example, a loan payable to a bank could be valued at the discounted amount of future cash flows using an entity's current incremental rate of borrowing for a similar liability; alternatively, the discount rate could be the rate that an entity would have to pay to a creditworthy third party to assume its obligation, with the creditor's legal consent (sometimes

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

referred to as the "settlement rate"), or the rate that an entity would have to pay to acquire essentially risk-free assets to extinguish the obligation in accordance with the requirements of Statement 76.

29. For deposit liabilities with defined maturities, such as certificates of deposit, an estimate of fair value might also be based on the discounted value of the future cash flows expected to be paid on the deposits. The discount rate could be the current rate offered for similar deposits with the same remaining maturities. For deposit liabilities with no defined maturities, paragraph 12 of this Statement requires that the fair value to be disclosed be the amount payable on demand at the reporting date.

Appendix B: ILLUSTRATIONS APPLYING THE DISCLOSURE REQUIREMENTS ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

30. The examples that follow are guides to implementation of the disclosure requirements of this Statement. Entities are not required to display the information contained herein in the specific manner illustrated. Alternative ways of disclosing the information are permissible as long as they satisfy the disclosure requirements of this Statement. Paragraphs 12 and 21 of this Statement describe possible additional voluntary disclosures that may be appropriate in certain circumstances.

Example 1—Financial Entity

31. Bank A might disclose the following:

Note V: Disclosures about Fair Value of Financial Instruments

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and short-term investments
For those short-term instruments, the carrying amount is a reasonable estimate of fair value.

Investment securities and trading account assets
For securities and derivative instruments held for trading purposes (which include bonds, interest rate futures, options, interest rate swaps, securities sold not owned, caps and floors, foreign currency contracts, and forward contracts) and marketable equity securities held for investment purposes, fair values are based on quoted market prices or dealer quotes. For other securities held as investments, fair value equals quoted market price, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

Loan receivables
For certain homogeneous categories of loans, such as some residential mortgages, credit card receivables, and other consumer loans, fair value is estimated using the quoted market prices for securities backed by similar loans, adjusted for differences in loan characteristics. The fair value of other types of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities.

Deposit liabilities
The fair value of demand deposits, savings accounts, and certain money market deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities.

Long-term debt
Rates currently available to the Bank for debt with similar terms and remaining maturities are used to estimate fair value of existing debt.

Interest rate swap agreements
The fair value of interest rate swaps (used for hedging purposes) is the estimated amount that the Bank would receive or pay to terminate the swap agreements at the reporting date, taking into account current interest rates and the current creditworthiness of the swap counterparties.

Commitments to extend credit, standby letters of credit, and financial guarantees written
The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of guarantees and letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date.

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

The estimated fair values of the Bank's financial instruments are as follows:

	19X9		19X8	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:				
Cash and short-term investments	$ XXX	$ XXX	$ XXX	$ XXX
Trading account assets	XXX	XXX	XXX	XXX
Investment securities	XXX	XXX	XXX	XXX
Loans	XXX		XXX	
Less: allowance for loan losses	(XXX)		(XXX)	
Loans, net of allowance	XXX	XXX	XXX	XXX
Financial liabilities:				
Deposits	XXX	XXX	XXX	XXX
Securities sold not owned	XXX	XXX	XXX	XXX
Long-term debt	XXX	XXX	XXX	XXX
Unrecognized financial instruments: *				
Interest rate swaps:				
In a net receivable position	XXX	XXX	XXX	XXX
In a net payabe position	(XXX)	(XXX)	(XXX)	(XXX)
Commitments to extend credit	(XXX)	(XXX)	(XXX)	(XXX)
Standby letters of credit	(XXX)	(XXX)	(XXX)	(XXX)
Financial guarantees written	(XXX)	(XXX)	(XXX)	(XXX)

Example 2—Nonfinancial Entity

[In this example, it is assumed that the carrying amounts of the short-term trade receivables and payables approximate their fair values.]

32. Corporation B might disclose the following:

Note X: Disclosures about Fair Value of Financial Instruments

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and short-term investments
The carrying amount approximates fair value because of the short maturity of those instruments.

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

Long-term Investments
The fair values of some investments are estimated based on quoted market prices for those or similar investments. For other investments for which there are no quoted market prices, a reasonable estimate of fair value could not be made without incurring excessive costs. Additional information pertinent to the value of an unquoted investment is provided below.

Long-term debt
The fair value of the Corporation's long-term debt is estimated based on the quoted market prices for the same or similar issues or on the current rates offered to the Corporation for debt of the same remaining maturities.

Foreign currency contracts
The fair value of foreign currency contracts (used for hedging purposes) is estimated by obtaining quotes from brokers.

The estimated fair values of the Corporation's financial instruments are as follows:

	19X9		**19X8**	
	Carrying Amount	**Fair Value**	**Carrying Amount**	**Fair Value**
Cash and short-term investments	$ XXX	$ XXX	$ XXX	$ XXX
Long-term investments for which it is:				
• Practicable to estimate fair value	XXX	XXX	XXX	XXX
• Not practicable	XXX	_____	XXX	_____
Long-term debt	(XXX)	(XXX)	(XXX)	(XXX)
Foreign currency contracts	XXX	XXX	(XXX)	(XXX)

It was not practicable to estimate the fair value of an investment representing 12 percent of the issued common stock of an untraded company; that investment is carried at its original cost of $XXX (19X8, $XXX) in the statement of financial position. At year-end, the total assets reported by the untraded company were $XXX (19X8, $XXX) and the common stockholders' equity was $XXX (19X8, $XXX), revenues were $XXX (19X8, $XXX), and net income was $XXX (19X8, $XXX).

Example 3—Small Nonfinancial Entity

33. Corporation C, whose only financial instruments are cash, short-term trade receivables and payables for which their carrying amounts approximate fair values, and long-term debt, might disclose the following:

Note Z: Long-Term Debt

Based on the borrowing rates currently available to the Corporation for bank loans with similar terms and average maturities, the fair value of long-term debt is $XXX (19X8, $XXX).

Copyright © 1991, Financial Accounting Standards Board
Not for redistribution

Appendix C

BACKGROUND INFORMATION AND BASIS FOR CONCLUSIONS

CONTENTS

Paragraph Numbers

Introduction 34
Background Information 35–36
Terminology 37
Disclosures about Fair Value of Financial Instruments 38–70
Relevance of Fair Value Information 39–50
Benefits and Costs 51–54
Level of Guidance 55–56
Financial Instruments with Quoted Prices 57–58
Financial Instruments with No Quoted Prices 59–63
Financial Liabilities 64–68
Core Deposits 69–70
Exclusion of Certain Financial Instruments 71–76
Application in Comparative Financial Statements 77–78
Applicability to Small, Nonpublic, or Nonfinancial Entities 79–81
Location of Information within Financial Reports 82–85
Applicability to Interim Financial Statements 86
Effective Dates and Transition 87–88

Appendix C: BACKGROUND INFORMATION AND BASIS FOR CONCLUSIONS

Introduction

34. This appendix summarizes considerations that Board members deemed significant in reaching the conclusions in this Statement. It includes reasons for accepting certain views and rejecting others. Individual Board members gave greater weight to some factors than to others.

Background Information

35. Following the issuance of Statement 105 in March 1990, the Board decided to focus primarily on disclosures about fair value as the second phase in the disclosure part of the financial instruments project. Background information on the financial instruments project and on the purposes of disclosure is provided in Appendix D of Statement 105.

36. On December 31, 1990, after discussing the issues in five public Board meetings and two public task force meetings, the Board issued the Exposure Draft, *Disclosures about Market Value of Financial Instruments* (1990 Exposure Draft). The Board received 204 comment letters on that Exposure Draft and 19 organizations and individuals presented their views during public hearings held on May 29 and 30, 1991. Also, eight entities participated in a field test of the disclosures proposed in the 1990 Exposure Draft. The field test results, which are kept confidential at the entities' request, were used by the Board during its deliberations on scope, display, and other issues addressed by this Statement.

Terminology

37. Some respondents to the 1990 Exposure Draft suggested that use of the term *market value* did not reflect adequately the broad range of financial instruments covered by this Statement. Those respondents associate the term *market value* only with items that are traded on active secondary markets (such as exchange and dealer markets). As highlighted by the discussion in paragraph 19 of this Statement, the Board does not make that distinction. The term *market value,* as defined in paragraph 5 of the 1990 Exposure Draft, is applicable whether the market for an item is active or inactive, primary or secondary. The Board decided, however, to use the term *fair value* in this Statement to avoid further confusion and also to be consistent with the terminology used in similar disclosure proposals made recently by other national and international standard-setting organizations. The concept of fair value is the same as that of market value in the 1990 Exposure Draft; those who associate the term *market value* only with items that are traded in active secondary markets may however prefer to consider fair value as a

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

broader concept that includes prices and rates obtained from both secondary and primary markets.

Disclosures about Fair Value of Financial Instruments

38. The Board decided to proceed with the second phase of the disclosure project because it has concluded that fair value provides a relevant measure for unrecognized financial instruments and another relevant measure for recognized financial instruments that are measured on other bases. The Board also concluded that the benefits of disclosing information about fair value, when practicable, justify the costs involved, except for certain financial instruments for which that information is not required by this Statement.

Relevance of Fair Value Information

39. Many respondents to the 1990 Exposure Draft questioned the relevance of measures of financial assets and liabilities based on fair values. The Board concluded that information about fair value of financial instruments meets the first objective of financial reporting stated in FASB Concepts Statement No. 1, *Objectives of Financial Reporting by Business Enterprises,* that is, to provide information that is useful to present and potential investors, creditors, and other users in making rational investment, credit, and similar decisions.

40. Fair values of financial instruments depict the market's assessment of the present value of net future cash flows directly or indirectly embodied in them, discounted to reflect both current interest rates and the market's assessment of the risk that the cash flows will not occur. Investors and creditors are interested in predicting the amount, timing, and uncertainty of future net cash inflows to an entity, as those are the primary sources of future cash flows from the entity to them. Periodic information about the fair value of an entity's financial instruments under current conditions and expectations should help those users both in making their own predictions and in confirming or correcting their earlier expectations.

41. Information about fair value better enables investors, creditors, and other users to assess the consequences of an entity's investment and financing strategies, that is, to assess its performance. For example, information about fair value shows the effects of a decision to borrow using fixed-rate rather than floating-rate financial instruments or of a decision to invest in long-term rather than short-term instruments. Also, in a dynamic economy, information about fair value permits continuous reassessment of earlier decisions in light of current circumstances.

42. Finally, several articles and reports in recent years have indicated the potential usefulness of information about market value of financial instruments, particularly as an indicator of the solvency of financial institutions. For example, a report issued by the U.S. Department of the Treasury in February 1991, *Modernizing the Financial System,* discusses the possible advantages of market value information for regulatory supervision of financial institutions.

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

43. Some respondents to the 1990 Exposure Draft argued that information about fair value of financial instruments is not relevant if an entity intends to hold them for the long term. They contend that, in those cases, the only relevant measure for a financial instrument is carrying value based on the amount initially paid or received (or perhaps a lower recoverable amount for an asset). They further argue that carrying value based on historical cost or proceeds provides relevant information because it focuses on the decision that creates the asset or liability, the earning effects of that decision that will be realized over time, and the ultimate recoverable or settlement value of the financial asset or liability. They also question the relevance of fair value measures because those measures focus on the effects of transactions and events that do not involve the entity. They reflect only "opportunity" gains and losses; "opportunities" that are not relevant unless they are intended to be realized.

44. The Board concluded that information about fair value of financial instruments, combined with information about carrying value, is relevant in part because it reflects the effects of management's decisions to buy a financial asset or incur a financial liability at a specific time, and then to continue to hold an asset or owe a liability. Deciding first on the best timing, based on existing market conditions, to acquire an asset or incur a liability and then when and how to realize gains or losses are important parts of management's stewardship responsibility to an entity's owners. Movements in fair values, and thus in market returns, during the period that a financial asset is held or a financial liability is owed provide a benchmark with which to assess the results of management's decisions and its success in maximizing the profitable use of an entity's economic resources and in minimizing financing costs.

45. Some respondents to the 1990 Exposure Draft argued that the subjectivity inherent in estimating the fair value of some financial assets and liabilities renders the information irrelevant and potentially misleading. Some also mentioned that many financial assets and liabilities are not readily marketable and that since it might be difficult or impossible to sell or settle them, information about their fair value is not useful.

46. The Board concluded that those arguments pertain more to the reliability of the estimates than to their relevance. In some cases, it may not be practicable to make a reasonable estimate of fair value. However, the Board expects that, in most cases, it will be practicable for an entity to make a reasonable estimate of fair value even of financial instruments that are not readily marketable.

47. Some have suggested that most or all financial instruments should be recognized and measured at their fair value in financial statements. The Board is considering recognition and measurement issues in other parts of the project on financial instruments. This Statement requires only disclosures about fair value.

48. The disclosures about fair value required by this Statement build on current practice and requirements. For example, FASB Statement No. 12, *Accounting for Certain Marketable Securities,* requires lower of cost or market measures and disclosure of the market value of

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

certain equity securities traded on exchanges or in the over-the-counter markets, and FASB Statement No. 15, *Accounting by Debtors and Creditors for Troubled Debt Restructurings,* provides guidance on determining the fair value of assets without active markets when transferred in settlement of troubled debt.

49. Other accounting standard-setting organizations have also concluded that fair value information about financial instruments is relevant. In September 1991, the International Accounting Standards Committee (IASC) issued an Exposure Draft, *Financial Instruments,* which, among other things, proposes disclosures about fair value for all financial instruments. The Exposure Draft is the result of a joint effort with the Canadian Institute of Chartered Accountants (CICA), which also issued an Exposure Draft, *Financial Instruments,* in September 1991.

50. The disclosures about fair value proposed in the IASC Exposure Draft are essentially the same as those required by this Statement. The CICA Exposure Draft also proposes disclosures about fair value, but only for financial assets; however, disclosures about fair value of financial liabilities are encouraged.

Benefits and Costs

51. One of the precepts of the Board's mission is to promulgate standards only when the expected benefits of the resulting information exceed the perceived costs. The Board strives to determine that a proposed standard will fill a significant need and that the costs entailed in satisfying that need, as compared with other alternatives, are justified in relation to the overall benefits of the resulting information. The benefits of providing fair value information are discussed in paragraphs 38-46 of this Statement.

52. The benefits of providing fair value information about financial instruments come at a cost—principally, the incremental cost of developing, implementing, and maintaining a measurement and reporting system to generate the required disclosures. The Board believes that many entities already have some systems in place to monitor and manage the market risk of their portfolios of financial instruments. The Board also believes that the incremental costs of the disclosure requirements of this Statement have been reduced in various ways: by introducing a notion of practicability to ensure that excessive costs will not be incurred solely to comply with the provisions of this Statement; by giving only general guidance on how to estimate fair value, so that an entity can exercise judgment in determining the most cost-efficient way of obtaining the information; by excluding certain financial instruments from the scope of the Statement because the benefits of providing fair value information about those instruments are at least uncertain in relation to the costs involved; and by delaying the effective date of application of this Statement for smaller entities that may need more time to be able to comply with the provisions of this Statement.

53. The Board realizes that by reducing some of the incremental costs of the requirements of this Statement in those ways, it also has reduced some of the benefits and possibly increased

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

other costs of those requirements. For example, by providing general rather than detailed guidance, it has potentially reduced the comparability of the fair value information among entities. At the same time, general guidance may increase the costs that will be incurred by preparers, auditors, regulators, and others as they evaluate and select appropriate approaches to assessing and disclosing fair value. Also, there will be a cost to users of financial statements as they attempt to make comparisons among entities of fair value information based on different methods and assumptions.

54. The Board is sensitive to the consequences that may occur as a result of the new information. For example, some respondents to the 1990 Exposure Draft and the 1987 Exposure Draft, *Disclosures about Financial Instruments,* mentioned that entities could possibly refrain from investing in financial instruments with significant market value volatility or in long-term instruments as a result of the required disclosures. Others mentioned that disclosing periodic changes in the fair value of all financial instruments of financial institutions might jeopardize the safety and soundness of the banking system as a whole. However, the nature and extent of those consequences are highly uncertain and are difficult to isolate from the effects of other events that will occur independent of that new information. For example, regulatory agencies for banks and thrifts recently have made and currently are considering further changes in regulations that may affect considerably the costs of doing business for those entities in the future. The Board's objective is not to enhance or diminish the possibility of those consequences but to improve disclosure of information about financial instruments so that users of financial statements may make better informed decisions.

Level of Guidance

55. Disclosures about fair value were originally proposed as part of a comprehensive set of disclosures about financial instruments included in the 1987 Exposure Draft. Some respondents to that Exposure Draft were concerned about the lack of specific guidance on how to estimate fair value. They maintained that different entities would disclose different market value estimates for similar financial instruments by using varying methods and assumptions, resulting in a lack of comparability between those entities' financial statements. Similar comments were made by some respondents to the 1990 Exposure Draft.

56. After considering those concerns, the Board reaffirmed its preference for general rather than detailed guidance in this Statement even though general guidance may result in disclosures that are less comparable from entity to entity. The Board concluded that the benefits to investors and creditors of having some timely information about fair value outweigh the disadvantage of that information being less than fully comparable. The Board noted that information about financial instruments based on historical prices also is not comparable from entity to entity. The Board also is aware that the current practices followed by entities that estimate fair value (as defined in this Statement) for internal management purposes vary and to impose specific methods or assumptions could increase the cost of compliance for at least some entities. Furthermore, those entities will be using methods they consider to be most pertinent to their

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

situation. Finally, financial instruments have such diverse characteristics that the Board believes that it is not practicable at this time to prescribe detailed methods and assumptions to be used in estimating fair value.

Financial Instruments with Quoted Prices

57. The Board concluded that quoted market prices provide the most reliable measure of fair value. Quoted market prices are easy to obtain and are reliable and verifiable. They are used and relied upon regularly and are well understood by investors, creditors, and other users of financial information. In recent years, new markets have developed and some existing markets have evolved from thin to active markets, thereby increasing the ready availability of reliable fair value information.

58. Although many respondents to the 1990 and 1987 Exposure Drafts agreed with the usefulness of disclosing quoted market prices derived from active markets, some argued that quoted prices from thin markets do not provide relevant measures of fair value, particularly when an entity holds a large amount of a thinly traded financial instrument that could not be absorbed by the market in a single transaction. The Board considered this issue and reiterated its belief that quoted prices, even from thin markets, provide useful information because investors and creditors regularly rely on those prices to make their decisions. The Board noted that providing the liquidation value of a block of financial instruments is not the objective of this Statement. The Board also concluded that requiring the use of available quoted market prices would increase the comparability of the disclosures among entities.

Financial Instruments with No Quoted Prices

59. The Board realizes that estimating fair value when quoted market prices are unavailable may, in some cases, require considerable judgment. However, the Board noted that a considerable degree of judgment also is needed when complying with other longstanding accounting and reporting requirements.

60. Many respondents to the 1990 and 1987 Exposure Drafts commented that some valuation techniques require sophisticated assumptions (for example, expected prepayments on a portfolio of loans assuming various future levels of interest rates) that would force entities, particularly smaller ones, to incur significant additional costs. The Board believes that simplified assumptions may sometimes be used (with appropriate disclosure) by an entity to provide a reliable estimate of fair value at a reasonable cost.

61. Paragraph 28 of the 1990 Exposure Draft stated that "an entity could also estimate market value by calculating separately (a) changes in market value due to changes in overall general interest rates and (b) changes in market value due to cash flows not expected to be collected and due to changes in market premiums for credit risk." Some respondents questioned whether that wording permitted the use of the allowance for loan losses in estimating the fair value of loans. Although the Board did not consider that specific issue at the Exposure Draft stage, some Board

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

members believe that the use of the allowance for loan losses would not provide an acceptable estimate of fair value in most cases because, according to current accounting literature, the allowance does not take into account the timing of the expected losses and all the potential losses due to credit risk. On the other hand, the factors considered in determining an appropriate allowance for loan losses are considered in determining the effects of changes in credit risk when estimating fair value. The Board decided to provide general rather than detailed guidance by stating, in paragraph 27 of Appendix A of this Statement, that adjustments to reflect the effects of changes in credit risk could be made by revising cash flow estimates, revising the discount rate, or some combination of both.

62. The Board is aware that it is not always practicable for an entity to estimate the fair value of a financial instrument or a category of financial instruments. The Board concluded that, in such cases, an entity should disclose the reasons fair value was not estimated and certain descriptive information pertinent to the value of those financial instruments that would help investors and creditors make their decisions. Examples of that information are the carrying amount of a financial instrument, the expected maturity, and the effective interest rate of the instrument.

63. Paragraph 14(c) of the 1990 Exposure Draft would have required an entity to state whether it believes the carrying amount approximates fair value or is significantly higher or lower than fair value. Many respondents objected to that requirement because they believe that, in most situations where it is not practicable to estimate fair value, it also would not be practicable to make such a statement. Also, they mentioned the risk of litigation arising from such a subjective disclosure. Based on those arguments, the Board decided not to include that disclosure requirement in this Statement.

Financial Liabilities

64. Some respondents to the 1990 Exposure Draft proposed excluding all financial liabilities from the scope of this Statement. Although most existing disclosures about fair value, and most discussion of the need for additional disclosures, have focused on the values of assets, the Board concluded that disclosures about the fair value of financial liabilities are important because market price volatility, which creates economic gains and losses, affects financial liabilities as well as assets. For example, a decline in the market price of an entity's bonds may give the entity an opportunity to settle the debt at a price below the carrying amount and, thus, to recognize a gain.

65. Some respondents to the 1990 Exposure Draft questioned the relevance of fair value information for liabilities when an entity does not have the intent or the ability to settle the debt. Some respondents argued that even when an entity intends to settle a debt to realize a gain due to an increase in market interest rates, there would be no economic gain if the cash needed for settlement is obtained through issuance of other debt at current higher rates. The Board believes that fair value information also is relevant in those cases because it helps users of financial

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

statements assess the effects on the entity of interest rate changes and the entity's ability to manage the related risk. The fair value of liabilities also provides information about the entity's success in minimizing financing costs on a continuing basis (for example, by timing borrowing decisions to take advantage of favorable market conditions). The Board noted that an entity does not necessarily need to settle a debt financed at a rate below prevailing market rates to realize a gain; the gain could be realized over the period of repayment of that debt. The Board also noted that under longstanding provisions of APB Opinion No. 26, *Early Extinguishment of Debt,* a gain is recognized in income if a debt is settled for less than its carrying amount, regardless of the source of the cash used to settle the debt.

66. Information about the fair values of both assets and liabilities is essential to permit an assessment of a financial institution's success in managing its financial assets and liabilities in a coordinated way. To limit potential net loss, financial institutions often seek to balance their asset and liability positions so that a decrease in the fair value of a financial asset is accompanied by a decrease in the fair value of a financial liability.

67. Some respondents, however, suggested that fair value information for liabilities of predominantly nonfinancial entities is not useful because those entities hold relatively few financial assets. Also, those liabilities are often incurred to finance the acquisition of nonfinancial assets; disclosing the changes in the fair value of financial liabilities without the corresponding changes in the fair value of nonfinancial assets may be misleading. The Board considered those arguments and reiterated its belief that fair value information for liabilities in itself is relevant information and should be provided. The Board acknowledges that the usefulness of the fair value information for liabilities would be enhanced by fair value information for nonfinancial assets but those assets are outside the scope of this Statement. This Statement, however, emphasizes that an entity may voluntarily disclose information about the fair value of its nonfinancial assets and liabilities (paragraph 12).

68. The Board acknowledges that, as for assets with no quoted prices, variations in the methods used to estimate the fair value of liabilities with no quoted prices might reduce the comparability of fair value information among entities. Some entities will estimate fair value by using an incremental rate of borrowing that considers changes in an entity's own credit risk, while others will use a settlement rate that ignores at least part of those credit risk changes. However, the Board concluded that it should not, at this time, prescribe a single method to be used for all unquoted liabilities. The Board currently has a project on its agenda on the uses of interest methods of accounting that examines questions about accounting measurements based on the present value of future economic benefits or sacrifices, and it will consider the question of a single method as part of that project. [4]

Core Deposits

69. Some respondents to the 1990 Exposure Draft commented that a financial institution should consider the value of its long-term customer relationships (core deposit intangibles) in

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

estimating the fair value of its deposits. The Board concluded that core deposit intangibles are separate intangible assets, not financial instruments, and are therefore outside the scope of this Statement. The Board noted that the accounting treatment for intangible assets similar to those identified by respondents as core deposit intangibles is partially addressed in FASB Statement No. 72, *Accounting for Certain Acquisitions of Banking or Thrift Institutions,* and the arguments used in Statement 72 support the conclusion reached by the Board in this Statement. The Board also noted that accounting standards do not prohibit voluntary disclosures about fair value of core deposit intangibles or any other assets or liabilities that are not included in the scope of this Statement.

70. Some respondents asked whether the Board's intention, in the 1990 Exposure Draft, was to prescribe the disclosure of the carrying amount of deposit liabilities as an estimate of their fair value. Others mentioned that the fair value of deposit liabilities may differ from their carrying amount even when, as required by paragraph 12 of this Statement, the value of core deposit intangibles is not taken into consideration; they suggested that those deposits represent an inexpensive source of funds that will be available for a considerable period of time. The Board decided that for deposit liabilities with no defined maturities, the fair value to be disclosed should be the amount payable on demand at the reporting date. The Board disagreed with the view that deposit liabilities should be valued using the rates available on more expensive alternative sources of funds because those rates are not relevant to the markets for deposits; also, that approach does not consider all the costs related to servicing the deposits.

Exclusion of Certain Financial Instruments

71. This Statement does not require disclosures about fair value for (a) employers' and plans' obligations for pension benefits, employers' and plans' obligations for other postretirement benefits including health care and life insurance benefits, employee stock option and stock purchase plans, and other forms of deferred compensation arrangements, (b) substantively extinguished debt subject to the disclosure requirements of Statement 76 and assets held in trust in connection with an in-substance defeasance of that debt, (c) insurance contracts, other than financial guarantees and investment contracts, (d) lease contracts, (e) warranty obligations and rights, (f) unconditional purchase obligations as defined in Statement 47, (g) investments accounted for under the equity method, (h) minority interests in consolidated subsidiaries, (i) equity investments in consolidated subsidiaries, and (j) equity instruments issued by the entity and classified in stockholders' equity in the statement of financial position.

72. Some disclosures about fair value are already required by existing generally accepted accounting principles for some items included in category (a) of the previous paragraph. In addition, a project on employee stock compensation plans is currently on the Board's agenda. In Statement 76, the Board concluded that meeting specified conditions effectively immunizes the obligation against market risk.

73. This Statement uses a definition of a financial instrument based on the definition

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

contained in Statement 105. During the Board's deliberations on this phase of the disclosure project, some questions arose about the application of the definition to contracts that involve the future delivery of goods or services. For example, Statement 105 excludes from the definition a contract that either requires the exchange of a financial instrument for a nonfinancial commodity (a forward contract) or permits settlement of an obligation by delivery of a nonfinancial commodity (an option), because those contracts involve the required or optional future exchange or delivery of an item that is not a financial instrument. An alternative approach would separate those contracts into financial and nonfinancial components; for example, a forward contract to purchase goods could be viewed as both an obligation to pay cash—a financial instrument—and a right to receive goods—not a financial instrument. If the financial component of that contract were subject to the disclosure requirements of this Statement, a further question would be whether the estimate of the fair value of the financial component should take into account changes in value caused by changes in the price of the underlying commodity. If not, difficulties would arise in distinguishing between changes in the fair value of the financial component and changes in the fair value of the nonfinancial component of the contract.

74. The Board concluded that disclosures about fair value should not be required for insurance contracts, lease contracts, warranty obligations, and unconditional purchase obligations (such as take-or-pay contracts). The Board believes that definitional and valuation difficulties are present to a certain extent in those contracts and obligations, and that further consideration is required before decisions can be made about whether to apply the definition to components of those contracts and whether to require disclosures about fair value for the financial components. The Board noted that issues about the application of the definition of a financial instrument are addressed more comprehensively in the November 1991 FASB Discussion Memorandum, *Recognition and Measurement of Financial Instruments.*

75. The other instruments listed in paragraph 71(g)-(j) were added as a result of comments received from respondents on the scope of the Statement. The disclosures were intended to apply only to financial assets and liabilities; therefore, minority interests in consolidated subsidiaries and an entity's own equity instruments classified in stockholders' equity are exempt from the disclosure requirements. The Board also decided to clarify that there is no requirement to disclose the fair value of investments in consolidated subsidiaries. Finally, the Board decided to exempt investments accounted for under the equity method from the disclosure requirements. The market value of those investments for which a quoted market price is available is already required to be disclosed under the provisions of Opinion 18, and the Board believes that the incremental benefits of estimating fair value for unquoted investments accounted for under the equity method do not outweigh the related costs.

76. Respondents to the 1990 Exposure Draft who proposed exempting other types of financial instruments from the disclosures required by this Statement were concerned about the difficulty or cost of estimating fair value. The Board concluded that no other type of financial instrument needs to be specifically excluded from the scope of this Statement because an entity will not be required to provide an estimate of fair value for a financial instrument if it is not practicable to do so.

Copyright © 1991, Financial Accounting Standards Board

Not for redistribution

Application in Comparative Financial Statements

77. The Board decided that, in the initial year of applying the provisions of this Statement, disclosures about fair value should be required as of the date of the latest statement of financial position. Obtaining prior-year fair value information not previously required might be difficult for many entities, and the Board believes the benefits would likely not justify the costs.

78. Although some respondents to the 1990 Exposure Draft suggested that the volume of disclosures would be unduly increased, the Board concluded that, after transition, comparative information about fair value should be provided for each year for which a statement of financial position is presented because that information is useful in assessing the management of market risk and pertinent trends.

Applicability to Small, Nonpublic, or Nonfinancial Entities

79. The Board considered whether certain entities should be excluded from the scope of this Statement. In particular, the Board considered the usefulness of the disclosures about fair value required by this Statement for small, nonpublic, or predominantly nonfinancial entities; a number of respondents to the 1990 Exposure Draft suggested exclusions on one or more of those bases. After considering the costs and benefits of those disclosures, the Board concluded that the disclosures are important and should be required for all entities, including small and nonpublic entities. The Board believes that the notion of "practicability" discussed in paragraph 15 ensures that excessive costs do not have to be incurred to comply with the disclosure requirements. In addition, the Board's decision to allow smaller entities additional time to apply the provisions of this Statement recognizes the fact that the costs of compliance can be reduced for those entities because the overall benefits of the information might be less than for larger entities.

80. The Board also concluded that while this Statement would likely have its greatest effect on the financial reporting of entities whose assets and liabilities are primarily financial instruments, financial instruments constitute an important part of the assets and liabilities of many predominantly nonfinancial entities as well, and disclosures about their fair value are useful and should be required. Furthermore, distinctions between financial and nonfinancial entities are becoming less pronounced.

81. The Board acknowledges that, for predominantly nonfinancial entities that have relatively few financial instruments, the benefits of disclosures about fair value might be less than for financial entities for which financial instruments are the most important part of their activities. However, the Board noted that the costs of compliance are relatively lower for those entities and that there are comparability benefits associated with having similar disclosure requirements apply to similar financial instruments. Accordingly, the Board decided that the disclosures required by this Statement should apply to all entities.

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

Location of Information within Financial Reports

82. The Board considered whether the disclosures required by this Statement should be part of the basic financial statements or should be provided as supplementary information. FASB Concepts Statement No. 5, *Recognition and Measurement in Financial Statements of Business Enterprises,* distinguishes between information that should be part of the basic financial statements and that which should be provided as supplementary information. Paragraph 7 of Concepts Statement 5 emphasizes that information disclosed as part of the basic financial statements amplifies or explains information recognized in financial statements and is essential to understanding that information.

83. Some respondents to the 1990 Exposure Draft suggested that the fair value information required by this Statement be disclosed as supplementary information because of the subjectivity associated with some estimates and to reduce the costs of compliance. Other respondents supported the Board's position in the Exposure Draft to allow entities enough flexibility to select the best way to disclose the information as part of the basic financial statements. Some also mentioned that the disclosures would be more credible if they are made as part of the basic financial statements.

84. The disclosures required by this Statement build on disclosures already included in basic financial statements and, like them, serve the major purposes of disclosure summarized in Appendix D of Statement 105; that is, to provide descriptions, to provide measures, and to help in assessing risks and potentials. In the past, requiring information to be supplementary has been done in conjunction with excluding certain entities from the scope of the requirements; however, as discussed in paragraphs 79-81, the Board concluded that the disclosures required by this Statement should be provided by all entities. The Board also concluded that all the disclosures about fair value of financial instruments should be included within the basic financial statements. The Board noted that having some fair value disclosures outside and others as part of the basic financial statements could potentially confuse the users of financial statements.

85. Some respondents believed that this Statement should require the fair value information to be disclosed in a tabular format in a single note to the financial statements. They believed that that approach would make the information more readily available and easier to understand by users of financial statements, thereby increasing the benefits of the disclosures. However, the Board concluded that entities should be allowed to determine the most appropriate way to disclose the fair value information in their financial statements.

Applicability to Interim Financial Statements

86. Some respondents to the 1990 Exposure Draft questioned whether the provisions of this Statement apply to interim financial statements. Paragraph 16 clarifies that disclosures about fair value are required to be made in all complete sets of interim financial statements, except in the

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

initial year of application of this Statement. The minimum disclosure requirements for summarized interim financial information issued by publicly traded entities are established by APB Opinion No. 28, *Interim Financial Reporting.* Since the provisions of this Statement do not amend Opinion 28, summarized interim financial information need not include the disclosures required by this Statement.

Effective Dates and Transition

87. Some respondents to the 1987 Exposure Draft mentioned that completion of the disclosure part of the financial instruments project would be desirable as soon as practicable so that the Board could proceed to focus entirely on recognition and measurement issues. On the other hand, many respondents expressed concern that some entities, particularly smaller ones, may not currently have in place the systems necessary to provide the required disclosures. After considering those comments, the Board proposed in the 1990 Exposure Draft that the effective date for larger entities, defined as entities with more than $100 million in total assets at the date of the latest statement of financial position, should be for financial statements issued for fiscal years ending after December 15, 1991. The Board also proposed to delay for one year the application of this Statement's requirements for entities that fall below that size criterion.

88. Many respondents to the 1990 Exposure Draft were concerned that they would not have sufficient time to prepare the required fair value information if a final Statement were issued late in 1991. Others suggested that the size criterion used to determine which entities would have additional time to implement the provisions of this Statement should be increased; some noted that bank regulators require less extensive information for banks with less than $150 million in total assets. After considering those comments, the Board concluded that larger entities, defined as entities with more than $150 million in total assets in the current statement of financial position, should apply the provisions of this Statement in financial statements issued for fiscal years ending after December 15, 1992. The Board decided to delay the effective date for smaller entities by an additional three years to provide sufficient time for those entities to develop the systems necessary to provide the required disclosures, in light of the experience gained by larger entities on the use of various methods and assumptions for estimating fair value.

Copyright © 1991, Financial Accounting Standards Board Not for redistribution

Footnotes

FAS107, Footnote 1--*Contractual obligations* encompass both those that are conditioned on the occurrence of a specified event and those that are not. All contractual obligations that are financial instruments meet the definition of *liability* set forth in FASB Concepts Statement No. 6, *Elements of Financial Statements,* although some may not be recognized as liabilities in financial statements--may be "off-balance-sheet"--because they fail to meet some other criterion for recognition. For some financial instruments, the obligation is owed to or by a group of entities rather than a single entity.

FAS107, Footnote 2--The use of the term *financial instrument* in this definition is recursive (because the term *financial instrument* is included in it), though it is not circular. The definition requires a chain of contractual obligations that ends with the delivery of cash or an ownership interest in an entity. Any number of obligations to deliver financial instruments can be links in a chain that qualifies a particular contract as a financial instrument.

FAS107, Footnote 3--*Contractual rights* encompass both those that are conditioned on the occurrence of a specified event and those that are not. All contractual rights that are financial instruments meet the definition of asset set forth in Concepts Statement 6, although some may not be recognized as assets in financial statements--may be "off-balance-sheet"--because they fail to meet some other criterion for recognition. For some financial instruments, the right is held by or the obligation is due from a group of entities rather than a single entity.

Footnote * Example 1—The amounts shown under "carrying amount" represent accruals or deferred income (fees) arising from those unrecognized financial instruments. Interest rate swaps and other derivative instruments entered into as trading activities are included in "trading account assets" or "securities sold not owned."

FAS107, Appendix C, Footnote 4--The Discussion Memorandum, *Present-Value-Based Measurements in Accounting,* was issued on December 7, 1990.

Copyright © 1991, Financial Accounting Standards Board Not for redistribution