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ALERT

FASB to Issue Additional Guidance for Recognition & Presentation of Other-Than-Temporary Impairments & Fair Value Measurements

The Financial Accounting Standards Board (FASB) has issued three new FASB Staff Positions (FSPs) to address concerns regarding: (1) determining whether a market is not active and a transaction is not orderly, (2) recognition and presentation of other-than-temporary impairments and (3) interim disclosures of fair value of financial instruments.

Determining whether a market is not active and a transaction is not orderly

The FSP provides additional guidance for estimating fair values in inactive markets. The originally proposed presumption that all transactions are distressed (not orderly) unless proven otherwise has been eliminated from the final draft. This FSP:

- Reinforces fair value for an asset in an inactive market is determined by the price that would be received to sell the asset in an orderly transaction (not a forced liquidation or distressed sale)
- Provides example indicators an entity may use to determine if a transaction is not orderly
- Includes an example that provides additional explanation on estimating fair value when the market activity for an asset has declined significantly
- Requires disclosure of any change in valuation technique and related inputs resulting from application of the FSP and quantification of its effects, if practical, by major category
- Applies to all fair value measurements to which FAS 157 is applicable

Recognition and presentation of other-than-temporary impairments

The FASB decided changes to existing guidance for determining whether impairment is other-than-temporary should be limited to debt securities. The impairment model for equity securities is unchanged by this FSP, although some new disclosure requirements do apply to equity securities. This FSP:

- Replaces the requirement that an entity's management must assert it has both the intent and the ability to hold an impaired security until recovery with a requirement that management assert:
  - It does not have the intent to sell the security; **and**
  - It is more-likely-than-not it will not have to sell the security before recovery of its cost basis
- Incorporates examples of factors to be considered in determining whether a credit loss exists and how those factors relate to the entity's assessment of the intent to sell and the likelihood of selling the security prior to recovering its cost basis
- Requires an entity to recognize the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income when the entity does not intend to sell the security and it is more-likely-than-not the entity will not have to sell the security before recovery of its cost basis
- Requires an entity to present the total of other-than-temporary impairment in income statements with an offset for the amount recognized in other comprehensive income
- Requires enhanced disclosures, including the methodology and key inputs used to measure an other-than-temporary impairment related to credit losses by major security type when only that portion of the impairment is reported in earnings
- Requires an entity to record, upon adoption, a cumulative-effect adjustment as of the beginning of the period of adoption to reclassify the noncredit component of a previously recognized other-than-temporary impairment from retained earnings to accumulated other comprehensive income if the entity does not intend

to sell the security and it is not more-likely-than-not that the entity will be required to sell the security before recovery

Interim disclosures about the fair value of financial instruments

This FSP amends FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*, to require disclosures about the fair value of financial instruments in interim financial statements, which were previously only required in annual financial statements. Public entities will be required to disclose on an interim basis the fair value amounts, as well as the methods and significant assumptions used to estimate the fair value of financial instruments. This FSP applies to all financial instruments within the scope of Statement 107. Nonpublic entities are excluded from the scope of this FSP.

Effective date

The FSPs will be effective for interim and annual periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. Entities will have several alternatives for adopting the rules:

- No early adoption of any of the three rules. In this instance, the entity will be required to adopt all three rules no later than periods ending after June 15, 2009
- Simultaneously early adopt the two FSPs addressing: (1) determining whether a market is not active and a transaction is not distressed and (2) recognition and presentation of other-than-temporary impairments
- Early adopt all three rules for periods ending after March 15, 2009. Adoption before this time period is prohibited

Entities that early adopt the FSP on interim disclosures related to fair value of financial instruments must adopt the other two FSPs at the same time

The information above is not a complete list of the provisions of these standards. These standards are complex and interact with existing standards. These FSPs will require careful consideration prior to and during implementation and we encourage you to contact your BKD advisor to discuss them in greater detail. ■

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