

## Contents

|                             |     |
|-----------------------------|-----|
| About the Authors .....     | iii |
| How to Use This Manual..... | v   |

## Introduction

### Chapter 1 Definitions of Fair Value

|   |        |
|---|--------|
| Highlights of Recent Accounting Announcements .....         | 1 — 2  |
| Methods for Determining Fair Value .....                    | 1 — 3  |
| Hierarchy of Fair Values .....                              | 1 — 4  |
| Exclusion From the Scope of the Fair Value Project .....    | 1 — 5  |
| Why Use Fair Value Rather Than Historical Cost? .....       | 1 — 5  |
| Why Is Fair Value More Relevant Than Historical Cost? ..... | 1 — 6  |
| Major Issues Surrounding a Mixed-Attribute Model .....      | 1 — 7  |
| Application of Fair Value in The current Environment .....  | 1 — 7  |
| Exhibit 1.1: Standards Incorporating Fair Value .....       | 1 — 10 |

### Chapter 2 Application of Fair Values in Reporting

|   |        |
|---|--------|
| Two Decades of Fair Value Issuances.....          | 2 — 1  |
| FASB'S Commitment to Fair Value .....             | 2 — 3  |
| Measurement of Fair Value .....                   | 2 — 4  |
| Fair Value Valuation Techniques .....             | 2 — 5  |
| Exhibit 2.1: Fair Value Valuation Hierarchy ..... | 2 — 5  |
| Income Approach .....                             | 2 — 6  |
| Revisions to Concepts Statement No. 7 .....       | 2 — 6  |
| Assumptions Underlying a Cash Flow Approach.....  | 2 — 11 |
| Market Approach .....                             | 2 — 11 |
| Estimating Exit Prices.....                       | 2 — 14 |
| Adjustments to Market Prices .....                | 2 — 15 |
| Cost Approach.....                                | 2 — 17 |

|  |        |
|--|--------|
| Hierarchy of Fair Value Estimations .....                | 2 — 18 |
| Level 1 Estimates .....                                  | 2 — 18 |
| Level 2 Estimates .....                                  | 2 — 19 |
| Level 3 Estimates .....                                  | 2 — 19 |
| Estimating Fair Value of Liabilities .....               | 2 — 19 |
| Strategic Considerations in Determining Fair Value ..... | 2 — 20 |
| Disclosures of Fair Value in Financial Statements .....  | 2 — 20 |

### **Chapter 3**

## **Regulatory Accounting Principles for Financial Institutions**

|   |        |
|---|--------|
| RAP in Financial Institutions .....                     | 3 — 1  |
| Regulatory Reports .....                                | 3 — 1  |
| Regulatory Reporting Requirements .....                 | 3 — 2  |
| Generally Accepted Accounting Principles .....          | 3 — 2  |
| Financial Accounting Standards Board .....              | 3 — 4  |
| Securities and Exchange Commission (SEC) .....          | 3 — 7  |
| International Accounting Standards Board (IASB) .....   | 3 — 8  |
| Public Company Accounting Oversight Board .....         | 3 — 8  |
| Levels of Authoritative Support for GAAP .....          | 3 — 9  |
| FDICIA .....  | 3 — 11 |
| FDIA Section 37 Provisions .....                        | 3 — 11 |
| Capital Adequacy Measurements .....                     | 3 — 13 |
| Sarbanes-Oxley Act of 2002 .....                        | 3 — 15 |
| Regulatory Requirements of Internal Control .....       | 3 — 16 |
| Management Reporting .....                              | 3 — 16 |
| Impact of SOX on Internal Control .....                 | 3 — 17 |
| Section 302 Certifications .....                        | 3 — 17 |
| Section 404 Certifications .....                        | 3 — 19 |
| Emerging Trends in Regulatory Reporting: Basel II ..... | 3 — 20 |
| Retail Credit Risk .....                                | 3 — 21 |
| Operational Risk .....                                  | 3 — 21 |
| Emerging Trends in Fair Value Accounting .....          | 3 — 22 |
| Fair Value Option .....                                 | 3 — 22 |
| Transfers of Financial Assets .....                     | 3 — 23 |
| Accounting for Hedging Activities .....                 | 3 — 23 |

**Assets**

**Chapter 4  
Accounting for the Fair Value of Cash and Cash Equivalents**

|   |       |
|---|-------|
| Types of Items Considered Cash or Cash Equivalents.....                 | 4 — 1 |
| Cash Items in the Process of Collection and Cash Equivalents .....      | 4 — 2 |
| Deposits with Other Depository Institutions.....                        | 4 — 2 |
| Balances with Federal Reserve Banks .....                               | 4 — 2 |
| Cash on Hand.....   | 4 — 2 |
| Reporting Cash and Cash Equivalents Information .....                   | 4 — 3 |
| Disclosures of Cash or Cash Equivalents Information.....                | 4 — 3 |
| In Preparing a Statement of Cash Flows for a Financial Institution..... | 4 — 4 |

**Chapter 5  
Investment Securities**

|   |        |
|---|--------|
| Overview of GAAP for Investment Securities.....                           | 5 — 1  |
| Held-to-Maturity (HTM) Securities.....                                    | 5 — 2  |
| Trading Securities .....  | 5 — 4  |
| AFS Securities.....   | 5 — 4  |
| Transfers Between Categories of Investments .....                         | 5 — 4  |
| Measuring Fair Value of Investments .....                                 | 5 — 4  |
| Classification as Current Assets.....                                     | 5 — 5  |
| Fair Value Definition .....   | 5 — 5  |
| Approximation of Fair Value.....  | 5 — 6  |
| Amortized Cost Defined.....   | 5 — 7  |
| Asset-Backed Securities.....  | 5 — 7  |
| Accounting for Income, Gains, and Losses from Security Transactions ..... | 5 — 8  |
| Reporting Income, Gains, and Losses in Fair Value Accounting .....        | 5 — 8  |
| Realized and Unrealized Gains and Losses Defined.....                     | 5 — 9  |
| Amortization of Premiums and Accretion of Discounts .....                 | 5 — 10 |
| Accretion of Discounts.....   | 5 — 11 |
| Special Issues Related to Accretion of Discounts .....                    | 5 — 11 |
| Zero Coupon Securities.....   | 5 — 11 |
| Accounting Guidelines.....  | 5 — 12 |
| Amortization of Premiums.....   | 5 — 13 |
| Sales Prior to Maturity — Recognizing Gains and Losses .....              | 5 — 13 |

|  |        |
|--|--------|
| Accounting Requirements for Specific Types of Investment Securities .....  | 5 — 14 |
| Investment Securities Obtained in Troubled Debt Restructurings .....   | 5 — 14 |
| Municipal Notes and Bonds .....  | 5 — 15 |
| Investments in Mortgage-Backed Securities .....  | 5 — 15 |
| Accounting for MBS Payments Received .....   | 5 — 17 |
| Accounting Requirements That Apply to Securities in a Trading Account .....  | 5 — 17 |
| Balance Sheet Classification .....   | 5 — 18 |
| Recording Market Values .....  | 5 — 18 |
| Trading Account Income .....   | 5 — 18 |
| Accounting for Derivative Investments .....  | 5 — 19 |
| Specific Disclosure Requirements Related to Derivatives .....  | 5 — 22 |
| Accounting for Certain Hybrid Financial Instruments .....  | 5 — 24 |
| The Fair Value Option for Financial Assets and Financial Liabilities .....   | 5 — 25 |
| Additional Disclosure Requirements Related to Derivatives That Are Established by<br>FASB Statement No. 161, Disclosures About Derivative Instruments and Hedging<br>Activities – an Amendment of FASB Statement No. 133 ..... | 5 — 26 |
| Specific Disclosures Required by FASB Statement No. 161 .....  | 5 — 27 |
| Amendments to Paragraph 44, FASB Statement No. 133 .....   | 5 — 27 |
| Amendments to Paragraphs 44C-44E of FASB Statement No. 133 .....   | 5 — 28 |
| FASB Statement No. 107, Disclosures about Fair Values of Financial Instruments .....   | 5 — 30 |
| APB Opinion No. 28, Interim Financial Reporting .....  | 5 — 30 |
| Accounting for Transfers of Financial Assets and Liabilities .....   | 5 — 31 |
| Accounting for Transfers and Servicing of Financial Assets as a Sale .....   | 5 — 33 |
| Accounting for the Transfer of Financial Assets as Secured Borrowings .....  | 5 — 33 |
| Extinguishments of Liabilities .....   | 5 — 34 |
| Specialized Areas Addressed by the EITF .....  | 5 — 34 |
| General Disclosures Required of Investments .....  | 5 — 36 |
| Exhibit 5.1: Accounting Treatment for Investment Securities .....  | 5 — 39 |
| Exhibit 5.2: Accounting for Transfers .....  | 5 — 40 |

## Chapter 6

### Accounting for Loans in a Financial Institution

|   |       |
|---|-------|
| Factors to Consider in Accounting for Loans .....             | 6 — 1 |
| Risk in a Loan Portfolio .....                                | 6 — 2 |
| Types of Lending .....  | 6 — 3 |
| Accounting for Loan Fees .....                                | 6 — 4 |
| Definition of Direct Loan Origination Fees .....              | 6 — 6 |
| Example of Accounting for Loan Fees .....                     | 6 — 7 |
| Loan Period Used for Amortization .....                       | 6 — 8 |
| Using the Interest Method to Amortize Net Deferred Fees ..... | 6 — 8 |
| Interest Rate Rises .....                                     | 6 — 9 |

|  |        |
|--|--------|
| Interest Rate Declines .....                               | 6 — 9  |
| Interest Rate Is Tied to an External Standard.....         | 6 — 10 |
| Financial Statement Classifications .....                  | 6 — 10 |
| When Loans Are Rewritten or Refinanced .....               | 6 — 10 |
| Purchases and Sales of Loans.....                          | 6 — 11 |
| General Observations on Accounting for Fees and Costs..... | 6 — 11 |
| Nonaccrual of Interest.....                                | 6 — 12 |
| Loan Loss Reserves and Provisions.....                     | 6 — 14 |
| Impairment of Loans .....                                  | 6 — 15 |
| Recognizing When a Loan Is Impaired.....                   | 6 — 16 |
| Measurement of Impairment.....                             | 6 — 17 |
| Accounting for Restructured Loans.....                     | 6 — 20 |
| Modification of Terms .....                                | 6 — 21 |
| Acceptance of Property .....                               | 6 — 21 |
| Restructuring with Acceptance of Property .....            | 6 — 21 |
| Restructuring with a New Loan Involved .....               | 6 — 22 |
| Accounting for Loan and Lease Losses.....                  | 6 — 22 |

## Chapter 7 Fixed Assets

|  |       |
|--|-------|
| Current Guidance .....                                   | 7 — 1 |
| Financial Accounting Standards Board.....                | 7 — 1 |
| Impaired Assets — FAS 121 .....                          | 7 — 1 |
| Changing Prices — FAS 133 .....                          | 7 — 2 |
| International Accounting Standards Committee .....       | 7 — 4 |
| American Institute of Certified Public Accountants ..... | 7 — 5 |
| Going Forward .....                                      | 7 — 6 |

## Chapter 8 Accounting for the Fair Value of Interest Receivable

|   |       |
|---|-------|
| Accounting for Interest Receivable Using RAP and GAAP ..... | 8 — 1 |
| Regulatory Accounting Principles .....                      | 8 — 1 |
| Generally Accepted Accounting Principles .....              | 8 — 2 |
| Nonaccrual of Interest.....                                 | 8 — 4 |
| Using Regulatory Accounting Principles.....                 | 8 — 4 |
| Treatment of Previously Accrued Interest Under RAP.....     | 8 — 4 |

## Chapter 9

### Other Assets

|   |        |
|---|--------|
| Servicing Assets Other Than Mortgage Loan Servicing Assets.....                         | 9 — 2  |
| Accounting for Servicing Assets.....  | 9 — 2  |
| Disclosures.....  | 9 — 3  |
| RAP Requirements for Servicing Assets and Liabilities.....                              | 9 — 4  |
| Identifiable Intangibles.....   | 9 — 4  |
| Accounting for Intangible Assets (Other Than Goodwill) Under GAAP.....                  | 9 — 4  |
| Disclosures About Acquired Intangible Assets and Goodwill.....                          | 9 — 5  |
| Disclosures When Impairment Loss Occurs.....  | 9 — 6  |
| Presentation of Intangible Assets, Including Goodwill, in the Financial Statements..... | 9 — 7  |
| RAP Accounting for Intangible Assets.....   | 9 — 7  |
| Valuation.....  | 9 — 8  |
| Fair Value Limitation.....  | 9 — 8  |
| Tier 1 Capital Limitations.....   | 9 — 8  |
| Sub-Limit to Tier 1 Capital.....  | 9 — 8  |
| Goodwill.....   | 9 — 9  |
| Accounting for Goodwill Under RAP.....  | 9 — 11 |
| Customers' Liabilities on Acceptances.....  | 9 — 12 |
| Deferred Tax Assets and Liabilities.....  | 9 — 12 |
| Deferred Tax Assets.....  | 9 — 12 |
| Deferred Tax Liabilities.....   | 9 — 13 |
| Accounting for Deferred Tax Assets and Liabilities Under RAP.....                       | 9 — 14 |
| Accounting for Miscellaneous Other Assets.....  | 9 — 15 |
| Recognizing Impairment of Other Assets.....   | 9 — 15 |
| Update on Accounting for Goodwill.....  | 9 — 17 |
| FAS 142, Goodwill and Other Intangible Assets.....                                      | 9 — 17 |
| FAS 141, Business Combinations.....   | 9 — 19 |
| FAS 72, Goodwill.....   | 9 — 20 |
| Update on Disclosure Requirements for Intangible Assets.....                            | 9 — 22 |
| Scope of the Project.....   | 9 — 22 |
| Issues Affecting the Application of Fair Value.....                                     | 9 — 23 |
| Accounting for the Fair Value of Nonmonetary Transactions.....                          | 9 — 23 |
| Definition of Productive Assets.....  | 9 — 25 |
| Accounting for the Fair Value of Nonperforming Assets.....                              | 9 — 25 |

**Liabilities**

**Chapter 10  
Accounting for the Fair Value of Deposits**

|  |        |
|--|--------|
| Accounting for Deposits Under GAAP .....                                   | 10 — 1 |
| Demand Deposits .....  | 10 — 1 |
| Savings Deposits .....   | 10 — 2 |
| Time Deposits .....  | 10 — 2 |
| Accounting for Deposits Under Regulatory Accounting Principles (RAP) ..... | 10 — 3 |
| Transaction Account .....  | 10 — 4 |
| Nontransaction Accounts .....  | 10 — 4 |
| Emerging Trends in Fair Value Accounting for Deposits .....                | 10 — 5 |
| International Accounting Projects .....                                    | 10 — 5 |
| Scope of Special Report .....  | 10 — 5 |
| Financial Accounting Standards Board .....                                 | 10 — 6 |

**Chapter 11  
Short-Term Borrowings**

|  |        |
|--|--------|
| Financial Accounting Standards Board ..... | 11 — 1 |
| Refinancing of Short-Term Debt .....       | 11 — 1 |
| Extinguishment of Debt .....               | 11 — 2 |
| Going Forward .....                        | 11 — 2 |

**Chapter 12  
Current Status of Fair Value Reporting Guidance**

|  |         |
|--|---------|
| Which Measure Is the Liquidation Basis? .....      | 12 — 5  |
| Financial Statement User Views on Fair Value ..... | 12 — 5  |
| Preliminary Views .....                            | 12 — 6  |
| Definition of Fair Value .....                     | 12 — 8  |
| Reporting Changes in Fair Value .....              | 12 — 10 |
| Issues Considered But Not Yet Resolved .....       | 12 — 10 |

|  |         |
|--|---------|
| Estimating Exit Prices for Financial Instruments Traded Only as Part of a Customer Relationship..... | 12 — 10 |
| Credit Card Relationships.....   | 12 — 11 |
| Demand Deposit Relationships.....  | 12 — 15 |
| Summary of the Issue.....  | 12 — 18 |
| Certain Credit Cards, Insurance Policies, and Warranties.....  | 12 — 18 |
| Single-Entity Credit Cards.....  | 12 — 19 |
| Certain Insurance Policies and Warranties.....   | 12 — 20 |
| Why Is This Issue Unresolved?.....   | 12 — 20 |
| FASB Proposed Statement on Fair Value Measurement.....   | 12 — 21 |
| Differences Between the Proposed Statement and Current Practice.....                                 | 12 — 22 |
| How the Proposed Statement Improves Financial Reporting.....   | 12 — 23 |
| How Conclusions Relate to the FASB’s Conceptual Framework.....                                       | 12 — 23 |
| Costs and Benefits of Applying the Proposed Statement.....   | 12 — 24 |
| Effective Date of the Proposed Statement.....  | 12 — 24 |
| Current Transactions.....  | 12 — 25 |
| Actual Current Transactions.....   | 12 — 26 |
| Hypothetical Current Transaction.....  | 12 — 27 |
| Willing Parties.....   | 12 — 27 |
| Reference Markets.....   | 12 — 28 |
| Transaction vs. Transportation Costs.....  | 12 — 29 |
| Assets — Inflows from Highest and Best Use.....  | 12 — 29 |
| Liabilities.....   | 12 — 30 |
| Outflows for Settlement.....   | 12 — 30 |
| Credit Standing.....   | 12 — 30 |
| Valuation Techniques.....  | 12 — 31 |
| Single vs. Multiple Techniques.....  | 12 — 32 |
| Undue Cost and Effort Criterion.....   | 12 — 32 |
| Present Value Techniques.....  | 12 — 33 |
| The Risk Adjustment.....   | 12 — 33 |
| Revision to Concepts Statement No. 7.....  | 12 — 34 |
| General Measurement Principle.....   | 12 — 34 |
| Fair Value Hierarchy.....  | 12 — 34 |
| Hierarchy Objective.....   | 12 — 35 |
| Level 1 Estimates.....   | 12 — 35 |
| Ability to Access.....   | 12 — 35 |
| Readily Available and Representative of Fair Value.....  | 12 — 36 |
| Readily Obtainable.....  | 12 — 36 |
| Level 1 Bid/Asked Spread Estimates — Pricing Methods.....  | 12 — 37 |
| Offsetting Positions.....  | 12 — 38 |
| Level 2 Estimates.....   | 12 — 39 |
| Level 3 Estimates.....   | 12 — 40 |
| Level 4 Estimates.....   | 12 — 40 |
| Effective Valuation Date.....  | 12 — 41 |
| Fair Value Option For Financial Assets and Financial Liabilities.....                                | 12 — 41 |
| Recent Announcements by the FASB.....  | 12 — 42 |

---

## Chapter 13 Other Liabilities

|  |        |
|--|--------|
| Calculating a Current Tax Liability .....                          | 13 — 1 |
| Valuation of Debt Assumed in a Purchase Business Combination ..... | 13 — 2 |

## Equities

## Chapter 14 Fair Value Accounting and Equity Accounts

|  |         |
|--|---------|
| Accounting for Unrealized Gains and Losses in Equity Accounts..... | 14 — 2  |
| Trading Securities .....   | 14 — 2  |
| Held to Maturity .....   | 14 — 2  |
| Available for Sale.....  | 14 — 3  |
| Specific Guidance on Capital Transactions.....                     | 14 — 4  |
| Regulatory Capital Requirements.....                               | 14 — 5  |
| Computation of Tier 1 Capital .....                                | 14 — 6  |
| Computation of Tier 2 Capital .....                                | 14 — 7  |
| Current Developments in Fair Value Accounting for Equities .....   | 14 — 7  |
| FAS 150.....   | 14 — 8  |
| Excluded from the Requirements of FAS 150 .....                    | 14 — 8  |
| Use of Fair Value in FAS 150.....                                  | 14 — 9  |
| Disclosure Requirements of FAS 150.....                            | 14 — 9  |
| Phase 2 in Liabilities and Equity Project .....                    | 14 — 10 |
| FAS 123R.....  | 14 — 10 |
| Changes to Current Practice.....                                   | 14 — 14 |

## **Financial Reporting**

### **Chapter 15 Fair Value Disclosure Requirements**

|  |        |
|--|--------|
| Development of Fair Value Accounting.....            | 15 — 2 |
| Disclosure and Recognition Requirements .....        | 15 — 3 |
| Statements of Financial Accounting Standards.....    | 15 — 3 |
| Fair Value Disclosures .....                         | 15 — 5 |
| General Requirements for Fair Value Disclosures..... | 15 — 5 |
| Specific Disclosures About Fair Value .....          | 15 — 7 |
| Exhibit 15.1: Assets .....                           | 15 — 9 |

### **Chapter 16 [Reserved]**

### **Miscellaneous**

### **Chapter 17 Miscellaneous Topics**

|  |         |
|--|---------|
| Hedging and Derivatives .....                      | 17 — 1  |
| Hedging .....                                      | 17 — 1  |
| Financial Derivatives .....                        | 17 — 1  |
| Products.....                                      | 17 — 3  |
| Derivatives Risks .....                            | 17 — 4  |
| Project on Revenue Recognition .....               | 17 — 6  |
| Scope and Objectives .....                         | 17 — 6  |
| Summary of Issues .....                            | 17 — 8  |
| Criteria for Recognition of Revenues.....          | 17 — 9  |
| Revenues .....                                     | 17 — 10 |
| Rights and Obligations.....                        | 17 — 11 |
| Fair Values of Assets and Liabilities.....         | 17 — 12 |
| Draft Recognition and Measurement Principles ..... | 17 — 13 |

|   |         |
|---|---------|
| Expected Output.....                              | 17 — 14 |
| History of the Project .....                      | 17 — 15 |
| Transfers of Financial Assets .....               | 17 — 18 |
| Disclosure Amendments for FAS 140 .....           | 17 — 18 |
| Consolidation of Variable Interest Entities ..... | 17 — 19 |

## Appendixes

### Appendix A Calculating Present Values

|  |        |
|--|--------|
| Appendix A — Calculating Present Values .....  | A — 1  |
| Present Value Analysis.....  | A — 1  |
| Future Value Formula .....   | A — 1  |
| Present Value Formula .....  | A — 2  |
| Present Value Calculations with Multiple Payments .....  | A — 2  |
| Calculating Bond Yields Using Present Value of Annuity Formulas .....  | A — 4  |
| Using Present Value Tables.....  | A — 5  |
| The Future Value of One Dollar .....   | A — 5  |
| The Future Value of a One Dollar Annuity.....  | A — 6  |
| Present Value of One Dollar .....  | A — 6  |
| Present Value of an Annuity .....  | A — 6  |
| Applications of Present Value Concepts in Accounting .....   | A — 7  |
| Statement of Financial Accounting Concepts No. 7, Using Cash Flow Information<br>and Present Value in Accounting Measurements..... | A — 8  |
| The Traditional vs. the Expected Cash Flow Approach.....   | A — 15 |
| Traditional Cash Flow Analysis.....  | A — 15 |
| Expected Cash Flow Analysis.....   | A — 15 |
| Exhibit A.1: Future Value of \$1 at the End of N Periods .....   | A — 17 |
| Exhibit A.2: Future Value of an Ordinary Annuity of \$1 per Period for<br>N Periods.....   | A — 18 |
| Exhibit A.3: Present Value of \$1/Future Value of \$1 at the End of N Periods.....   | A — 19 |
| Exhibit A.4: Present Value of an Ordinary Annuity of \$1 per Period for<br>N Periods.....  | A — 21 |

**Appendix B**  
**Determining Fair Value in a Financial Institution**

|   |       |
|---|-------|
| Examples of the Determination of Fair Value in a Bank ..... | B — 2 |
| Exceptions to Fair Value Disclosures .....                  | B — 3 |

**Appendix C**  
**Model Chart of Accounts Referenced by Chapter Numbers**

|                                |       |
|--------------------------------|-------|
| Assets .....                   | C — 1 |
| Liabilities.....               | C — 1 |
| Equity .....                   | C — 2 |
| Income and Expenses .....      | C — 2 |
| Other Noninterest Expense..... | C — 3 |