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Preface

December 2019

We are pleased to present A Roadmap to Fair Value Measurements and Disclosures (Including the Fair Value Option), which provides an overview of the accounting and disclosure guidance in ASC 820 and ASC 825 as well as insights into how to apply this guidance in practice.

Fair value measurements and disclosures are generally relevant to the financial reporting of all entities. The guidance on this topic in ASC 820 primarily reflects the outcome of the FASB’s joint project with the International Accounting Standards Board (IASB®) to substantially converge U.S. GAAP and IFRS® Standards. The FASB has made certain amendments since the culmination of its joint project with the IASB, including those in (1) ASU 2016-01, which amends the guidance in U.S. GAAP on the classification and measurement of financial instruments and certain disclosure requirements associated with the fair value of financial instruments, and (2) ASU 2018-13, which changes the fair value disclosure requirements for all entities. The guidance in this Roadmap is written as if adoption of ASU 2016-01 has occurred. Chapter 11 discusses fair value disclosures required before and after ASU 2018-13.

The guidance on application of the fair value option originated in FASB Statement 159. The FASB has not made any significant amendments to this guidance since the issuance of the original pronouncement.

This Roadmap is intended to help entities navigate the accounting guidance related to fair value measurements and disclosures, reduce complexity, and arrive at appropriate accounting conclusions.

Subscribers to the Deloitte Accounting Research Tool (DART) may access any interim updates to this publication by selecting the document from the “Roadmaps” tab on DART’s home page. If a “Summary of Changes Since Issuance” displays, subscribers can view those changes by clicking the related links or by opening the “active” version of the Roadmap.

We hope you find this Roadmap a useful resource, and we welcome your suggestions for future improvements. If you need assistance with applying the fair value guidance or have other questions about this topic, we encourage you to consult our technical specialists and other professional advisers.

Sincerely,

Deloitte & Touche LLP
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1.1 Introduction
Many Codification topics in U.S. GAAP require or permit fair value measurements or disclosures about fair value measurements (as well as fair-value-based measurements, such as fair value less costs to sell, or disclosures about those measurements). This chapter gives an overview of the principles in ASC 820 and of the concepts related to fair value measurements under U.S. GAAP. For a discussion of the scope of ASC 820, see Chapter 2.

1.2 Objective of a Fair Value Measurement

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<td><strong>05-01</strong> This Topic contains only the Overall Subtopic. This Topic does all of the following:</td>
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<td>a. Defines fair value</td>
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<td>b. Sets out in a single Topic a framework for measuring fair value</td>
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<td>c. Requires disclosures about fair value measurements.</td>
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<tr>
<td><strong>05-01A</strong> This Topic explains how to measure fair value for financial reporting. It does not require fair value measurements in addition to those already required or permitted by other Topics and is not intended to establish valuation standards or affect valuation practices outside of financial reporting.</td>
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<td><strong>05-01B</strong> Fair value is a market-based measurement, not an entity-specific measurement. For some assets and liabilities, observable market transactions or market information might be available. For other assets and liabilities, observable market transactions and market information might not be available. However, the objective of a fair value measurement in both cases is the same—to estimate the price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions (that is, an exit price at the measurement date from the perspective of a market participant that holds the asset or owes the liability).</td>
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<td><strong>05-01C</strong> When a price for an identical asset or liability is not observable, a reporting entity measures fair value using another valuation technique that maximizes the use of relevant observable inputs and minimizes the use of unobservable inputs. Because fair value is a market-based measurement, it is measured using the assumptions that market participants would use when pricing the asset or liability, including assumptions about risk. As a result, a reporting entity's intention to hold an asset or to settle or otherwise fulfill a liability is not relevant when measuring fair value.</td>
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<td><strong>05-1D</strong> The definition of fair value focuses on assets and liabilities because they are a primary subject of accounting measurement. In addition, this Topic shall be applied to instruments measured at fair value that are classified in shareholders' equity.</td>
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Before the issuance of FASB Statement 157 (the pre-Codification fair value standard that preceded ASC 820), various definitions of fair value existed in U.S. GAAP and the guidance on applying those definitions was limited. Statement 157 addressed the need for the consistency and comparability of fair value measurements and for expanded disclosures about those measurements. Specifically, Statement 157 (codified in ASC 820) contained a single definition of fair value, established a principles-based framework for measuring fair value that can be used by all entities, and required entities to provide relevant disclosures about fair value measurements. The definition of fair value and the measurement framework apply to assets, liabilities, and items classified in stockholders’ equity.

ASC 820 emphasizes that fair value is a market-based measurement based on an exit price notion and is not entity-specific. Therefore, a fair value measurement must be determined on the basis of the assumptions that market participants would use in pricing an asset or liability, whether those assumptions are observable or unobservable. The fair value hierarchy in ASC 820 serves as a basis for considering market-participant assumptions and distinguishes between (1) market-participant assumptions developed on the basis of market data that are independent of the entity (observable inputs) and (2) an entity’s own assumptions about market-participant assumptions developed on the basis of the best information available in the particular circumstances, including assumptions about risk inherent in inputs or valuation techniques (unobservable inputs). In accordance with the fair value hierarchy, entities are required to maximize the use of relevant observable inputs and minimize the use of unobservable inputs. This focus on the observability of inputs also often affects the valuation technique used to measure fair value.

The single definition of fair value, the fair value measurement framework, and the disclosure requirements in ASC 820 are intended to result in increased consistency and comparability of fair value measurements (as well as disclosures about fair value measurements). Such consistency and comparability should result in information that financial statement users (e.g., present and potential investors, creditors, regulators, and others) find useful in making investment, credit, and similar decisions. The fair value disclosure requirements are intended to increase the transparency of the inputs and valuation techniques used in fair value measurements; however, an entity will need to tailor its fair value disclosures to meet the needs of users of its financial statements, depending on whether it is a public business entity or a nonpublic entity.

### 1.2.1 Exit Price

**ASC 820-10**

30-2 When an asset is acquired or a liability is assumed in an exchange transaction for that asset or liability, the transaction price is the price paid to acquire the asset or received to assume the liability (an entry price). In contrast, the fair value of the asset or liability is the price that would be received to sell the asset or paid to transfer the liability (an exit price). Entities do not necessarily sell assets at the prices paid to acquire them. Similarly, entities do not necessarily transfer liabilities at the prices received to assume them.

**Definition of Fair Value**

35-2 This Topic defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

**ASC 820-10 — Glossary**

**Exit Price**

The price that would be received to sell an asset or paid to transfer a liability.
The fundamental principle underlying the definition of fair value and the fair value measurement framework is that a fair value measurement represents an exit price, which ASC 820-10-35-2 describes as “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.” Thus, a fair value measurement is not entity-specific. Furthermore, a “mark-to-model” measurement that does not include an adjustment for risk does not represent a fair value measurement if market participants would include such an adjustment in pricing the related asset or liability (i.e., a fair value measurement must reflect all relevant factors that market participants would consider in determining a price for an asset or liability). ASC 820 also specifies that the fair value of an item classified in stockholders’ equity is similarly determined from the perspective of a market participant that holds the identical item as an asset as of the measurement date (i.e., also on the basis of an exit price determined from the perspective of the holder of the identical item as an asset).

Note that a transaction price (i.e., an entry price) differs from an exit price. As discussed in Chapter 9, when an item is initially measured at fair value, this measurement should represent an exit price in the principal market in which an entity would transact or, in the absence of a principal market, the most advantageous market. Accordingly, the exit price notion is applied consistently to both initial and subsequent measurements at fair value.

Paragraphs C51 and C52 in the Basis for Conclusions of Statement 157 further clarify why the exit price notion is the basis of fair value measurements:

Respondents indicated that the guidance in the Exposure Draft was ambiguous about when a price in an actual transaction that involves the reporting entity should be used to measure the fair value of an asset or liability at initial recognition. Many of those respondents referred to related practice issues under Issue 02-3 (and its guidance in footnote 3 for fair value measurements at initial recognition). In its redeliberations, the Board considered that issue largely in the context of the related guidance in paragraphs 7 and 27 of Concepts Statement 7, which state:

At initial recognition, the cash or equivalent amount paid or received (historical cost or proceeds) is usually assumed to approximate fair value, absent evidence to the contrary.

A transaction in the marketplace — an exchange for cash at or near to the date of the transaction — is the most common trigger for accounting recognition, and accountants typically accept actual exchange prices as fair value in measuring those transactions, absent persuasive evidence to the contrary. Indeed, the usual condition for using a measurement other than the exchange price is a conclusion that the stated price is not representative of fair value. [Footnote reference omitted.]

In this Statement, the Board clarified that in situations in which the reporting entity acquires an asset or assumes a liability in an exchange transaction, the transaction price represents the price paid to acquire the asset or received to assume the liability (an entry price). The fair value of the asset or liability represents the price that would be received to sell the asset or paid to transfer the liability (an exit price). Conceptually, entry and exit prices are different. Entities do not necessarily sell or otherwise dispose of assets at the prices paid to acquire them. Similarly, entities do not necessarily transfer liabilities at the prices paid to assume them. The Board agreed that in many cases the transaction price will equal the exit price and, therefore, represent the fair value of the asset or liability at initial recognition, but not presumptively (a change to Concepts Statement 7). This Statement includes examples of factors the reporting entity should consider in determining whether a transaction price represents the fair value of the asset or liability at initial recognition. The Board plans to consider those factors in assessing the appropriate measurement attribute at initial recognition in individual accounting pronouncements on a project-by-project basis.

1.3 History of Fair Value Requirements

Since the issuance of Statement 157 (codified in ASC 820), the FASB has amended its fair value requirements a number of times. Notably, the Board issued ASU 2011-04 in May 2011 as part of its effort to converge its fair value measurement and disclosure requirements with those of the IASB, which released its counterpart standard, IFRS 13, in the same month. (However, while U.S. GAAP and IFRS Standards on fair value are now largely converged, certain differences remain. See Appendix B for a summary of those differences.)
Table 1-1 summarizes the significant amendments made to the fair value measurement and disclosure guidance since the issuance of Statement 157.¹

<table>
<thead>
<tr>
<th>Standard</th>
<th>Principal Amendments Made</th>
</tr>
</thead>
<tbody>
<tr>
<td>FSP FAS 157-1</td>
<td>Excluded from the scope of the fair value measurement guidance the use of fair value for lease classification or measurement purposes.</td>
</tr>
<tr>
<td>FSP FAS 157-2</td>
<td>Delayed the effective date of Statement 157 for nonfinancial assets and nonfinancial liabilities, except for those items that are recognized or disclosed at fair value in the financial statements on a recurring basis.</td>
</tr>
<tr>
<td>FSP FAS 157-3</td>
<td>Clarified the application of the fair value measurement guidance in an inactive market and provided a related illustrative example. Subsequently superseded by FSP FAS 157-4.</td>
</tr>
<tr>
<td>FSP FAS 157-4</td>
<td>Provided additional guidance on estimating fair value when the volume and level of activity for an asset or liability have significantly decreased and includes guidance on identifying circumstances in which a transaction is not orderly.</td>
</tr>
<tr>
<td>FSP FAS 132(R)-1</td>
<td>Provided guidance on an employer's fair value disclosures about plan assets of a defined benefit pension or other postretirement plan.</td>
</tr>
<tr>
<td>ASU 2009-05</td>
<td>Clarifies guidance on the fair value measurement of liabilities. Significant amendments include:</td>
</tr>
<tr>
<td></td>
<td>• In circumstances in which a quoted price in an active market for an identical liability is not available, an entity should measure fair value by applying (1) a valuation technique that uses the quoted price of the identical liability when traded as an asset (a Level 1 measurement) or quoted prices for similar liabilities or similar liabilities when traded as assets or (2) another valuation technique that is consistent with the fair value measurement principles in ASC 820.</td>
</tr>
<tr>
<td></td>
<td>• In measuring the fair value of a liability, an entity is not required to include a separate input or adjustment to other inputs related to the existence of a restriction that prevents that entity from transferring the liability.</td>
</tr>
<tr>
<td>ASU 2009-12</td>
<td>Provides a practical expedient for the fair value measurement of investments in entities that calculate NAV per share or its equivalent. This practical expedient allows entities to measure fair value on the basis of the investment's NAV per share provided that the NAV of the investment is calculated in a manner consistent with the measurement guidance in ASC 946, including measurement of all or substantially all of the underlying investments of the investee in accordance with ASC 820. Requires entities to provide additional disclosures by category of investment, including information about redemption restrictions and unfunded commitments.</td>
</tr>
<tr>
<td>ASU 2009-16</td>
<td>Eliminates the practicability exceptions that allowed for (1) the use of the transaction price (an entry price) to measure the fair value, at initial recognition, of financial assets and liabilities under ASC 860 and (2) an exemption to the requirement to measure fair value if it is not practicable to do so for financial assets obtained and financial liabilities incurred in a sale under ASC 860.</td>
</tr>
<tr>
<td>ASU 2010-06</td>
<td>Amends ASC 820 to require new disclosures about (1) transfers between Levels 1 and 2 of the fair value hierarchy and (2) activity in the Level 3 rollforward. Also clarifies existing disclosure requirements related to (1) the level of disaggregation of classes of assets and liabilities and (2) inputs and valuation techniques used in fair value measurements. Note that several of these disclosure requirements were amended and simplified by later ASUs.</td>
</tr>
</tbody>
</table>

¹ Table 1-1 does not address certain insignificant amendments related to (1) conforming changes to definitions associated with other Codification topics, (2) minor conforming amendments resulting from changes made to other Codification topics, (3) minor technical corrections, and (4) maintenance updates.
### Principal Amendments Made

<table>
<thead>
<tr>
<th>Standard</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>ASU 2011-04</td>
<td>Amends ASC 820 to converge many of the fair value measurement and disclosure requirements in U.S. GAAP with those in IFRS Standards. Since IFRS 13 was developed on the basis of Statement 157, the amendments in this ASU primarily constitute (1) nonsubstantive wording changes to many of the fair value measurement and disclosure requirements in ASC 820 and other U.S. GAAP or (2) clarifications of the FASB’s intended application of these requirements. Specific amendments made by ASU 2011-04 include (1) introducing the concept of measuring the fair value of financial instruments that are managed within a portfolio on a net basis in certain circumstances, (2) applying premiums and discounts in a fair value measurement on the basis of the unit of account, and (3) requiring additional disclosures about fair value measurements (i.e., valuation process and sensitivity disclosures for Level 3 measurements, use of a nonfinancial asset that differs from its highest and best use, and the categorization by level within the fair value hierarchy for items that are not measured at fair value but for which fair value must be disclosed). Note that several of these disclosure requirements were amended and simplified by later ASUs.</td>
</tr>
<tr>
<td>ASU 2012-04</td>
<td>Clarifies the fair value disclosure requirements applicable to certain nonpublic entities.</td>
</tr>
<tr>
<td>ASU 2012-07</td>
<td>Eliminates the requirement that an entity incorporate into fair value measurements used in the impairment tests of unamortized film costs the effects of any changes in estimates resulting from the consideration of subsequent evidence if the information would not have been considered by market participants as of the measurement date. These amendments align the impairment assessment of unamortized film costs with the definition of fair value in ASC 820 because, to the extent that uncertainties are resolved or other information becomes known after the balance sheet date but before the financial statements are issued or available to be issued, such effects should not be incorporated with certainty into the fair value measurement as of the balance sheet date unless market participants would have made such assumptions. The ASU also clarifies that a valuation model used as of the measurement date should incorporate assumptions that market participants would have made about the uncertainty in timing and amount of cash flows as of the measurement date in accordance with ASC 820. Note that although the amendments in this ASU were made to ASC 926, they provide guidance that is relevant to the application of ASC 820 by analogy.</td>
</tr>
<tr>
<td>ASU 2013-03</td>
<td>Clarifies that the requirement to disclose the level of the fair value hierarchy within which fair value measurements are categorized in their entirety (i.e., Level 1, 2, or 3) does not apply to nonpublic entities for items that are not measured at fair value but for which fair value is disclosed.</td>
</tr>
<tr>
<td>ASU 2013-09</td>
<td>Defers indefinitely certain requirements to disclose quantitative information about the significant unobservable inputs used in Level 3 fair value measurements for investments held by a nonpublic employee benefit plan in its plan sponsor’s own nonpublic-entity equity securities, including equity securities of its plan sponsor’s nonpublic affiliated entities.</td>
</tr>
<tr>
<td>ASU 2014-13</td>
<td>Allows an entity that consolidates a CFE to elect to measure the financial assets and financial liabilities of the CFE by using a measurement alternative. Under the measurement alternative, the entity measures both the financial assets and the financial liabilities of the CFE by using the more observable of the fair value of the financial assets or the fair value of the financial liabilities.</td>
</tr>
<tr>
<td>ASU 2015-07</td>
<td>Removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured by using the practical expedient related to NAV per share.</td>
</tr>
<tr>
<td>Standard</td>
<td>Principal Amendments Made</td>
</tr>
<tr>
<td>------------------</td>
<td>------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>ASU 2015-10</td>
<td>Makes the following amendments to ASC 820:</td>
</tr>
<tr>
<td></td>
<td>• Removes the practical expedient that allowed certain NFP entities not to recognize certain items at fair value if fair value cannot be measured with sufficient reliability.</td>
</tr>
<tr>
<td></td>
<td>• Clarifies that a change in price selected within a bid-ask spread is subject to the general accounting and disclosure guidance in ASC 820 on changes in valuation techniques.</td>
</tr>
<tr>
<td></td>
<td>• Clarifies that the disclosures for nonrecurring fair value measurements are provided as of the date of the measurement and not as of the period-end.</td>
</tr>
<tr>
<td>ASU 2016-01</td>
<td>Amends the fair value disclosure requirements to:</td>
</tr>
<tr>
<td></td>
<td>• Require public business entities that are required to disclose the fair value of financial instruments measured at amortized cost on the balance sheet to measure those fair values by using the exit price notion in a manner consistent with ASC 820, thereby eliminating the entry price method previously used by some entities for fair value disclosures of certain financial assets.</td>
</tr>
<tr>
<td></td>
<td>• Removes the practicability exception that allowed entities to avoid providing certain fair value disclosures for financial instruments under ASC 825 if it is impractical to determine fair value.</td>
</tr>
<tr>
<td></td>
<td>• Eliminates the requirement for entities other than public business entities to provide certain disclosures about the fair value of financial instruments that are not recognized at fair value on the balance sheet.</td>
</tr>
<tr>
<td>ASUs 2018-03 and 2019-04</td>
<td>made additional amendments to ASU 2016-01 that affect fair value measurements of equity securities without readily determinable fair values; however, those amendments did not affect ASC 820.</td>
</tr>
<tr>
<td>ASU 2016-02</td>
<td>Requires that fair value measurements under ASC 842 conform to the fair value measurement guidance in ASC 820. This guidance was later affected by ASU 2019-01.</td>
</tr>
<tr>
<td>ASU 2016-19</td>
<td>Clarifies the difference between a valuation approach (i.e., cost, market, income) and a valuation technique and requires specific disclosures at the valuation technique level.</td>
</tr>
<tr>
<td>ASU 2018-09</td>
<td>Clarifies that when measuring the fair value of a liability or item classified in stockholders’ equity on the basis of the fair value of the corresponding asset from the perspective of a market participant that holds the identical item as an asset, any restrictions that affect the fair value of the asset should also be included in the fair value measurement of the liability or equity instrument.</td>
</tr>
<tr>
<td>ASU 2018-13</td>
<td>Simplifies and improves financial statement disclosures as part of the FASB’s disclosure effectiveness initiative. This ASU amends ASC 820 to (1) remove several fair value disclosure requirements, (2) modify certain disclosure requirements, and (3) add certain disclosure requirements for public business entities. See Chapter 11 for discussion of the ASC 820 disclosures an entity is required to provide before and after adopting this ASU.</td>
</tr>
</tbody>
</table>
Chapter 2 — Scope

2.1 Scope and Scope Exceptions

2.1.1 General

ASC 820-10

Overall Guidance

15-1 The Scope Section of the Overall Subtopic establishes the scope for the Fair Value Measurement Topic. Except as noted below, this Topic applies when another Topic requires or permits fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements).

Other Considerations

Topics and Subtopics Not Within Scope

15-2 The Fair Value Measurement Topic does not apply as follows:

a. To accounting principles that address share-based payment transactions (this includes Subtopic 505-50 and all Subtopics in Topic 718 except for 718-40, which is within the scope of Topic 820)

b. To Sections, Subtopics, or Topics that require or permit measurements that are similar to fair value but that are not intended to measure fair value, including both of the following:
   1. Sections, Subtopics, or Topics that permit measurements that are determined on the basis of, or otherwise use, standalone selling price
   2. Topic 330.

c. To accounting principles that address fair value measurements for purposes of lease classification or measurement in accordance with Topic 840. This scope exception does not apply to assets acquired and liabilities assumed in a business combination or an acquisition by a not-for-profit entity that are required to be measured at fair value in accordance with Topic 805, regardless of whether those assets and liabilities are related to leases.

d. To the recognition and measurement of revenue from contracts with customers in accordance with Topic 606

e. To the recognition and measurement of gains and losses upon the derecognition of nonfinancial assets in accordance with Subtopic 610-20.
### Pending Content (Transition Guidance: ASC 820-10-65-1)

15-2 The Fair Value Measurement Topic does not apply as follows:

a. To accounting principles that address share-based payment transactions (this includes Subtopic 505-50 and all Subtopics in Topic 718 except for 718-40, which is within the scope of Topic 820)
b. To Sections, Subtopics, or Topics that require or permit measurements that are similar to fair value but that are not intended to measure fair value, including both of the following:
   1. Sections, Subtopics, or Topics that permit measurements that are determined on the basis of, or otherwise use, standalone selling price
   2. Topic 330.
c. Subparagraph superseded by Accounting Standards Update No. 2016-02.
d. To the recognition and measurement of revenue from contracts with customers in accordance with Topic 606
e. To the recognition and measurement of gains and losses upon the derecognition of nonfinancial assets in accordance with Subtopic 610-20.

### Pending Content (Transition Guidance: ASC 718-10-65-11)

15-2 The Fair Value Measurement Topic does not apply as follows:

a. To accounting principles that address share-based payment transactions (this includes all Subtopics in Topic 718 except for 718-40, which is within the scope of Topic 820)
b. To Sections, Subtopics, or Topics that require or permit measurements that are similar to fair value but that are not intended to measure fair value, including both of the following:
   1. Sections, Subtopics, or Topics that permit measurements that are determined on the basis of, or otherwise use, standalone selling price
   2. Topic 330.
c. Subparagraph superseded by Accounting Standards Update No. 2016-02.
d. To the recognition and measurement of revenue from contracts with customers in accordance with Topic 606
e. To the recognition and measurement of gains and losses upon the derecognition of nonfinancial assets in accordance with Subtopic 610-20.

ASC 820 establishes a framework for measuring fair value and requires disclosures about fair value measurements. ASC 820 does not, however, include any requirements related to initially or subsequently measuring an item at fair value. Rather, with certain exceptions, ASC 820 applies when another Codification topic requires or permits fair value measurements or disclosures about fair value measurements.

Sections 2.1.2 and 2.1.3 discuss the scope of ASC 820’s measurement and disclosure requirements. Section 2.2 discusses practicability exceptions afforded by ASC 820. Section 2.3 discusses the application of ASC 820 to specific assets, liabilities, equity instruments, and transactions.
2.1.2 Measurement

With certain exceptions (see Sections 2.2 and 2.3), the measurement guidance in ASC 820 applies whenever another FASB Codification topic uses the phrase “fair value” to describe how an entity is required or permitted to measure financial and nonfinancial assets and liabilities, instruments classified in a reporting entity's stockholders’ equity, or specific transactions, regardless of whether this measurement pertains to initial or subsequent recognition or to disclosure. Fair value measurements that are within the scope of ASC 820 include measurements at (1) fair value less costs to sell and (2) the lower of fair value or cost. However, ASC 820 does not apply to measurement objectives under other Codification topics when such objectives are related to an amount similar to fair value but are not intended to represent a fair value measurement (e.g., measurement objectives related to share-based payment arrangements and revenue recognition). When another Codification topic requires that an item be measured at an allocated amount on the basis of relative fair value or by using a residual allocation approach based on fair value, the item is not measured at a fair value amount. However, any fair value amount used in such allocation should be determined in accordance with the measurement guidance in ASC 820 in the absence of a specific exception in the Codification topic requiring such measurement.

Table 2-1 describes other Codification topics that require or permit an entity to measure a recognized item at fair value on the basis of the fair value measurement guidance in ASC 820. Note the following regarding the items in this table:

- The table only includes items that are initially or subsequently measured at (1) fair value, (2) fair value less costs to sell, or (3) the lower of fair value or cost. (For more information about the specific type of fair value measurement, see the Codification paragraphs identified in the table.) The table does not include items initially or subsequently measured at (1) relative fair value, (2) a residual amount after the deduction of an item measured at fair value, or (3) an incremental amount on the basis of the change in fair value of an item that is not subsequently recognized at fair value and that has not been subject to a modification.

- The table does not address situations in which other Codification topics require an entity to determine the appropriate accounting for an item or a transaction on the basis of a fair value measurement. For example, the table does not cover the requirement to use fair value in determining whether (1) an asset is impaired, (2) an acquisition or disposition involves a business, (3) an entity is a VIE or an investment company, (4) an investment is accounted for under the equity method, (5) a lease is classified as operating or capital, (6) an equity-linked instrument or instrument settleable in an issuer's equity shares is classified within equity, and (7) a convertible instrument contains a beneficial conversion feature. The table also does not address the use of a fair value measurement solely to calculate EPS. In such circumstances, the measurement guidance in ASC 820 applies unless the Codification topic contains a specific exception that permits an entity not to apply ASC 820.

- The table does not include transition guidance that applies to certain Codification subtopics. To determine any applicable transition guidance, see the specific Codification paragraphs identified in the table.

1 ASC 820 does not, however, apply to measurements based on the lower of cost or market value, such as measurements of inventory under ASC 330.
## Table 2-1

<table>
<thead>
<tr>
<th>ASC Subtopic</th>
<th>Initial Measurement or Subsequent Nonrecurring Fair Value Measurement</th>
<th>Subsequent Recurring Fair Value Measurement</th>
</tr>
</thead>
</table>
| 260-10      | • Dividend for the difference between the (1) fair value of the consideration transferred to holders of preferred stock and (2) carrying amount of the preferred stock (ASC 260-10-S99-2).<sup>2</sup>  
• Dividend and offsetting entry for the fair value of the additional consideration issued when a convertible preferred stock instrument is converted in accordance with an inducement offer (ASC 260-10-S99-2). |                                            |
| 310-10      | • Notes receivable (ASC 310-10-30-5 and 30-6).  
• Standby commitments to purchase loans that are accounted for as written options (ASC 310-10-30-7 and ASC 310-10-35-46).  
• Impairment loss on a collateral-dependent loan receivable measured on the basis of the fair value of the collateral (ASC 310-10-35-22 and ASC 310-10-35-32).  
• Nonmortgage loans held for sale (ASC 310-10-35-48).  
• Mortgage or nonmortgage loans transferred into the held-for-sale classification (ASC 310-10-35-49).<sup>2</sup> |                                            |

---

<sup>2</sup> ASC 820-10-50-2(a) states that “[n]onrecurring fair value measurements . . . are those that other Topics require or permit in the statement of financial position in particular circumstances (for example, when a reporting entity measures a long-lived asset or disposal group classified as held for sale at fair value less costs to sell in accordance with Topic 360 because the asset’s fair value less costs to sell is lower than its carrying amount.)” In some cases, an item may be remeasured to fair value in consecutive reporting periods; however, such remeasurement is a nonrecurring fair value measurement because the other Codification topic that requires or permits such measurement does not require or permit the measurement for all changes in fair value. For example, a long-lived asset or disposal group classified as held for sale may be remeasured to fair value less costs to sell in each financial reporting period until its disposal because the fair value less costs to sell declines in each financial reporting period. However, such measurement is not a recurring fair value measurement because ASC 360 does not allow an entity to remeasure a long-lived asset or disposal group classified as held for sale at a fair value amount that exceeds the asset’s (or disposal group’s) original cost basis. In the absence of a specific exception, the disclosure requirements in ASC 820 apply to items subsequently measured at fair value on a nonrecurring basis (see Sections 2.3, 11.2.2.1, and 11.3.2.1 for more information). Conversely, the disclosure requirements in ASC 820 do not apply to items that are initially measured at fair value. Other Codification topics may, however, require specific disclosures regarding initial measurements at fair value under ASC 820 (see Appendix A for more information).

<sup>3</sup> ASC 820-10-50-2(a) states that “[r]ecurring fair value measurements . . . are those that other Topics require or permit in the statement of financial position at the end of each reporting period.” In the absence of a specific exception, the disclosure requirements in ASC 820 apply to items subsequently measured at fair value on a recurring basis (see Sections 2.3, 11.2.2.1, and 11.3.2.1 for more information).
(Table continued)

<table>
<thead>
<tr>
<th>ASC Subtopic</th>
<th>Initial Measurement or Subsequent Nonrecurring Fair Value Measurement</th>
<th>Subsequent Recurring Fair Value Measurement</th>
</tr>
</thead>
</table>
| 310-40       | • Asset receivable from a purchaser that substitutes the original debtor in a troubled debt restructuring (ASC 310-40-40-1).  
• Asset received from a debtor in full satisfaction of a receivable in a troubled debt restructuring (ASC 310-40-40-2 through 40-4 and ASC 310-40-55-7).  
• Asset recognized for foreclosed property received in a troubled debt restructuring (ASC 310-40-40-7).  
• Debt security of the original debtor received as a full or partial settlement in a troubled debt restructuring (ASC 310-40-40-8A and 40-9). |                                                                 |
| 320-10       | • Impairment loss on an available-for-sale or held-to-maturity debt security that an investor intends to sell or more likely than not will be required to sell before recovery of the security's amortized cost basis less any current-period credit loss (ASC 320-10-35-34B).  
• Transfer of a debt security between categories (ASC 320-10-35-10 through 35-10B). | • Investments in a trading or available-for-sale debt security (ASC 320-10-35-1 and ASC 320-10-35-36).  
• Investments in a structured note (ASC 320-10-35-38(h)). |
| 321-10       | • Investment in an equity security that (1) does not have a readily determinable fair value and is accounted for by using the practical expedient in ASC 321-10-35-2 upon the occurrence of (a) an observable price change or (b) an impairment loss or (2) was accounted for by using the practical expedient in ASC 321-10-35-2 and (a) subsequently has a readily determinable fair value or (b) is elected to be accounted for at fair value (ASC 321-10-35-2 through 35-5). | • Investment in an equity security that (1) has a readily determinable fair value or (2) does not have a readily determinable fair value and is not accounted for by using the practical expedient in ASC 321-10-35-2 (ASC 321-10-35-1). |
| 323-10       | • Retained (obtained) investment in common stock of an investee (including a joint venture) in a deconsolidation (derecognition) transaction (ASC 323-10-30-2).  
• The difference between (1) the fair value of contingent consideration issued or issuable and (2) the liability amount recorded for such contingent consideration (ASC 323-10-35-14A).  
• Impairment loss on an equity method investment (ASC 323-10-35-31 and 35-32). |                                                                 |
**Items That an Entity Is Required or Permitted to Recognize at Fair Value in Accordance With ASC 820**

<table>
<thead>
<tr>
<th>ASC Subtopic</th>
<th>Initial Measurement or Subsequent Nonrecurring Fair Value Measurement</th>
<th>Subsequent Recurring Fair Value Measurement</th>
</tr>
</thead>
</table>
| 325-30       | • Stock received from a demutualization (ASC 325-30-30-1AA).          | • Investment in a life-settlement contract that is accounted for by using the fair value method (ASC 325-30-25-2 and ASC 325-30-35-12).
|              | • Impairment loss on an investment in a life-settlement contract that is accounted for by using the investment method (ASC 325-30-35-11).⁴ |                                           |
| 325-40       | • Investment in a beneficial interest in securitized financial assets held by a transferor (ASC 325-40-30-1). | • Investment in a beneficial interest in securitized financial assets that is classified as trading (ASC 325-40-25-2). |
|              | • Impairment loss on a beneficial interest in securitized financial assets that is not classified as trading (ASC 325-40-35-13). |                                           |
| 326-10       | • Financial instruments within the scope of ASC 326-20, other than held-to-maturity debt securities, when the FVO in ASC 825 is elected (ASC 326-10-65-1(i)). | • Financial instruments within the scope of ASC 326-20, other than held-to-maturity debt securities, when the FVO in ASC 825 is elected (ASC 326-10-65-1(i)). |
| 326-20       | • Expected credit losses on a collateral-dependent financial asset that is measured on the basis of the fair value of the collateral (ASC 326-20-35-4 and 35-5 and ASC 326-20-45-4). |                                           |
|              | • Expected credit losses on financial assets secured by collateral maintenance provisions (ASC 326-20-35-6). |                                           |
|              | • A valuation allowance once a decision is made to sell a loan not currently classified as held-for-sale (ASC 326-20-35-7). |                                           |
| 326-30       | • Impairment loss on an available-for-sale debt security that an investor intends to sell or more likely than not will be required to sell before recovery of its amortized cost basis (ASC 326-30-35-10). |                                           |
| 350-20       | • Impairment loss on goodwill equal to the excess of the carrying amount of an entity (or reporting unit) over its fair value (ASC 350-20-35-8 and ASC 350-20-35-72 and 35-73). |                                           |

⁴ See Section 2.3.10 for more information about life-settlement contracts accounted for under ASC 325-30.

⁵ See footnote 4.
### Items That an Entity Is Required or Permitted to Recognize at Fair Value in Accordance With ASC 820

<table>
<thead>
<tr>
<th>ASC Subtopic</th>
<th>Initial Measurement or Subsequent Nonrecurring Fair Value Measurement</th>
<th>Subsequent Recurring Fair Value Measurement</th>
</tr>
</thead>
</table>
| 350-30       | • Intangible asset acquired individually or with a group of assets in a transaction other than a business combination (ASC 350-30-25-4).<sup>6</sup>  
• Impairment losses on an intangible asset (ASC 350-30-35-14 and ASC 350-30-35-19).<sup>6</sup> | |
| 350-40       | • Impairment loss on a computer software asset that is being developed for internal use and for which it is no longer probable that the asset will be completed and placed into service (ASC 350-40-35-3). | |
| 360-10       | • Acquired interest in the residual value of a leased asset (ASC 360-10-30-3 and 30-4).  
• Impairment loss on an acquired interest in the residual value of a leased asset (ASC 360-10-35-14).  
• Impairment loss on a long-lived asset (asset group) classified as held and used (ASC 360-10-35-17 and ASC 360-10-45-13).<sup>7</sup>  
• Impairment loss on a long-lived asset (disposal group) classified as held for sale (ASC 360-10-35-40 and ASC 360-10-35-43).<sup>8</sup>  
• Impairment loss on a long-lived asset (disposal group) that is disposed of in an exchange or spin-off (ASC 360-10-35-40-4).<sup>9</sup> | |
| 405-20       | • Guarantee obligation of a debtor that is released from being primarily obligated and becomes secondarily liable on a debt instrument (ASC 405-20-40-2). | |
| 410-20       | • Each layer of an asset retirement obligation (ARO) (ASC 410-20-25-7 and ASC 410-20-35-1).<sup>10</sup> | |

<sup>6</sup> Finite-lived intangible assets may be tested for impairment as part of an asset group. Any impairment loss is allocated to the finite-lived intangible assets on a relative fair value basis.

<sup>7</sup> See Section 2.3.7 for more information about the impairment of long-lived assets (asset groups) under ASC 360-10.

<sup>8</sup> See footnote 7.

<sup>9</sup> See footnote 7.

<sup>10</sup> See Section 2.3.9 for discussion of a practical expedient related to the fair value measurement of an ARO under ASC 410-20.
### Items That an Entity Is Required or Permitted to Recognize at Fair Value in Accordance With ASC 820

<table>
<thead>
<tr>
<th>ASC Subtopic</th>
<th>Initial Measurement or Subsequent Nonrecurring Fair Value Measurement</th>
<th>Subsequent Recurring Fair Value Measurement</th>
</tr>
</thead>
</table>
| 420-10 11    | • Liability for a cost associated with an exit or disposal activity (ASC 420-10-30-1).  
                        • Liability for one-time employee termination benefits (ASC 420-10-25-9 and ASC 420-10-30-4 through 30-6).  
                        • Liability for a cost to terminate a contract before the end of its term (ASC 420-10-30-7 and 30-8).  
                        • Liability for a cost that will continue to be incurred under a contract without an economic benefit to the entity (ASC 420-10-30-9).  
                        • Liability for other costs associated with an exit or disposal activity (ASC 420-10-30-10). |                                             |
| 460-10       | • Guarantee liabilities (ASC 460-10-30-2). 12                          |                                             |
| 470-20       | • Share-lending arrangement on an entity’s own common shares (ASC 470-20-25-20A and ASC 470-20-30-26A).  
                        • Liability for a convertible instrument issued as repayment of a nonconvertible instrument at the nonconvertible instrument’s maturity (ASC 470-20-30-19).  
                        • Liability for a convertible instrument issued for cash proceeds when the purchaser also provides (receives) goods or services to (from) the issuer (ASC 470-20-30-26).  
                        • Liability component of a convertible instrument subject to the cash conversion guidance (ASC 470-20-30-27 and ASC 470-20-40-25).  
                        • Expense and offsetting entry to APIC when it is probable that a counterparty to a share-lending arrangement will default (ASC 470-20-35-11A).  
                        • Adjustment to equity for the difference between the amount previously recognized in equity and the fair value of the conversion option in a convertible debt instrument upon reclassification of the conversion option from equity to an embedded derivative liability (ASC 470-20-35-19). |                                             |

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11 See Section 2.3.13 for discussion of an exception to the fair value measurement requirements under ASC 420-10.
12 See Section 2.3.4 for discussion of a practical expedient related to this fair value measurement under ASC 460-10.
<table>
<thead>
<tr>
<th>ASC Subtopic</th>
<th>Initial Measurement or Subsequent Nonrecurring Fair Value Measurement</th>
<th>Subsequent Recurring Fair Value Measurement</th>
</tr>
</thead>
<tbody>
<tr>
<td>470-20</td>
<td>• Issuance of equity securities to settle a debt instrument in accordance with the debt instrument's original conversion terms if the debt instrument did not contain a substantive conversion feature (ASC 470-20-40-5(b)).&lt;br&gt;• Consideration exchanged upon settlement of a convertible instrument subject to the cash conversion guidance (ASC 470-20-40-20(a)).&lt;br&gt;• Expense and offsetting entry for the fair value of the additional consideration issued when a convertible debt instrument is converted in accordance with an inducement offer (ASC 470-20-40-16 and ASC 470-20-40-26).</td>
<td></td>
</tr>
<tr>
<td>470-30</td>
<td>• Participation liability when a lender is entitled to participate in the appreciation of the market value of a mortgaged real estate project (ASC 470-30-25-1 and ASC 470-20-30-1).</td>
<td>• Participation liability when a lender is entitled to participate in the appreciation of the market value of a mortgaged real estate project (ASC 470-30-35-4A).</td>
</tr>
<tr>
<td>470-50</td>
<td>• Modified or exchanged debt instrument when the original and new debt instruments are substantially different (ASC 470-50-40-13).&lt;br&gt;• Increase in the fair value of an embedded conversion option in a modification or exchange of a convertible debt instrument that does not represent an extinguishment (ASC 470-50-40-15).</td>
<td></td>
</tr>
<tr>
<td>470-60</td>
<td>• Gain equal to the excess of the carrying amount of a payable over the fair value of assets transferred to a creditor when a debtor transfers assets in full satisfaction of a payable in a troubled debt restructuring (ASC 470-60-35-2).&lt;br&gt;• Gain or loss for the difference between the fair value and carrying amount of assets transferred by a debtor to a creditor to fully or partially settle a payable in a troubled debt restructuring (ASC 470-60-35-3 and ASC 470-60-35-8).&lt;br&gt;• Equity interest issued by a debtor to a creditor to fully settle a payable in a troubled debt restructuring (ASC 470-60-35-4).</td>
<td></td>
</tr>
</tbody>
</table>
### Items That an Entity Is Required or Permitted to Recognize at Fair Value in Accordance With ASC 820

<table>
<thead>
<tr>
<th>ASC Subtopic</th>
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<th>Subsequent Recurring Fair Value Measurement</th>
</tr>
</thead>
<tbody>
<tr>
<td>480-10</td>
<td>• Mandatorily redeemable financial instruments (ASC 480-10-30-1).</td>
<td>• Liability for contingent consideration in a business combination (ASC 480-10-35-4A).</td>
</tr>
<tr>
<td></td>
<td>• Conditionally redeemable financial instruments that become mandatorily redeemable (ASC 480-10-30-2).</td>
<td>• Financial instruments recognized under ASC 480-10-25 that are not subject to another measurement attribute under ASC 480-10 or another Codification topic (ASC 480-10-35-5).</td>
</tr>
<tr>
<td></td>
<td>• Liability and reduction to equity for a forward contract that must be physically settled by repurchase of a fixed number of the issuer's equity shares in exchange for cash (ASC 480-10-30-3 through 30-5).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Financial instruments recognized under ASC 480-10-25 (ASC 480-10-30-7).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Initial carrying amount of a redeemable equity instrument (ASC 480-10-S99-3A).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Subsequent measurement of an equity instrument redeemable at fair value (ASC 480-10-S99-3A).</td>
<td></td>
</tr>
<tr>
<td>505-20</td>
<td>• Adjustment to retained earnings, capital stock, and APIC for a stock dividend (ASC 505-20-30-3).</td>
<td></td>
</tr>
<tr>
<td>505-30</td>
<td>• Purchase of treasury shares (ASC 505-30-30-3).</td>
<td></td>
</tr>
<tr>
<td>710-10</td>
<td>• Deferred compensation liability for Plans B and C (ASC 710-10-35-3).</td>
<td></td>
</tr>
<tr>
<td>712-10</td>
<td>• Plan assets (ASC 712-10-35-1).</td>
<td></td>
</tr>
</tbody>
</table>
| 715-30       | • Projected benefit obligation upon the occurrence of a settlement, curtailment, or termination benefit (ASC 715-30-35-81 and ASC 715-30-55-76). | • Plan assets (ASC 715-30-35-50).<sup>15</sup>  
• Participation rights (ASC 715-30-35-58).<sup>16</sup>  
• Other contracts with insurance entities (ASC 715-30-35-60). |
| 715-60       | • Plan assets (ASC 715-60-35-107).<sup>17</sup>  
• Participation rights (ASC 715-60-35-116).<sup>18</sup>  
• Other contracts with insurance entities (ASC 715-60-35-120). | |

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<sup>13</sup> See Section 2.3.17 for more information about deferred compensation arrangements held in rabbi trusts accounted for under ASC 710-10.  
<sup>14</sup> See Section 2.3.15 for more information about plan assets and obligations accounted for under ASC 712-10.  
<sup>15</sup> See Section 2.3.15 for more information about plan assets and obligations accounted for under ASC 715-30.  
<sup>16</sup> See Section 2.3.15 for more information about the measurement of a participation right under ASC 715-30.  
<sup>17</sup> See Section 2.3.15 for more information about plan assets and obligations accounted for under ASC 715-60.  
<sup>18</sup> See Section 2.3.15 for more information about the measurement of a participation right under ASC 715-60.
### Items That an Entity Is Required or Permitted to Recognize at Fair Value in Accordance With ASC 820

<table>
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</table>
| 715-70       | • Compensation expense at the time of an allocation to participants by a defined contribution plan that received assets from a terminated defined benefit plan (ASC 715-70-55-7).  
              |                                                           | • Debt security of a third party or the employer included in the unallocated assets of a defined contribution plan that received assets from a terminated defined benefit plan (ASC 715-70-55-9). |
| 715-80       | • Noncash contribution to a multiemployer plan (ASC 715-80-35-1).       |                                             |
| 718-40       | • The number of shares released to settle a liability related to a specified or determinable benefit to employees that is funded through an ESOP (ASC 718-40-25-14).  
              |                                                           | • Compensation cost and the credit to equity for committed-to-be-released shares of a leveraged ESOP (ASC 718-40-30-1 through 30-4).  
              |                                                           | • Compensation cost and the credit to equity for shares contributed or committed to be contributed to a nonleveraged ESOP (ASC 718-40-30-5).  
              |                                                           | • Purchase of suspense shares from an ESOP (ASC 718-40-40-6).  
              |                                                           | • Compensation cost equal to the fair value of shares as of the date on which debt of a leveraged ESOP is extinguished (ASC 718-40-40-7). |
| 720-25       | • Contribution expense (ASC 720-25-25-2 and ASC 720-25-30-1).19        |                                             |
| 730-10       | • Tangible and intangible research and development assets acquired in a business combination or an acquisition by an NFP entity, regardless of whether such assets have an alternative future use (ASC 730-10-15-4(f)). |                                             |
| 730-20       | • Warrant or similar instrument issued in a research and development arrangement (ASC 730-20-25-12). |                                             |

19 See Section 2.3.18 for more information about contributions made accounted for under ASC 720-25.
<table>
<thead>
<tr>
<th>ASC Subtopic</th>
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<th>Subsequent Recurring Fair Value Measurement</th>
</tr>
</thead>
<tbody>
<tr>
<td>740-10</td>
<td>• Acquired financial asset and acquired asset held for disposal in an asset purchase (ASC 740-10-25-51(a)).</td>
<td></td>
</tr>
<tr>
<td>805-10</td>
<td>• Previously held equity interest in a business combination achieved in stages (ASC 805-10-25-10).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Gain or loss on a settlement of a preexisting noncontractual relationship (ASC 805-10-55-21(a)).</td>
<td></td>
</tr>
<tr>
<td>805-20</td>
<td>• Contingent consideration arrangement of an acquiree that is assumed by an acquirer in a business combination (ASC 805-20-25-15A and ASC 805-20-30-9A).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Indemnification asset of an acquirer in a business combination that is related to an asset or liability recognized as of the acquisition date and measured at the acquisition-date fair value (ASC 805-20-25-27 and ASC 805-20-30-18).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Identifiable assets acquired, liabilities assumed, and any noncontrolling interest in an acquiree in a business combination (ASC 805-20-30-1).</td>
<td></td>
</tr>
<tr>
<td>805-30</td>
<td>• Contingent consideration transferred as part of the consideration in a business combination, regardless of whether the consideration is classified as an asset, a liability, or an equity instrument (ASC 805-30-25-5).</td>
<td>• Contingent consideration transferred as part of the consideration in a business combination, when the consideration is classified as an asset or liability instrument (ASC 805-30-35-1).</td>
</tr>
<tr>
<td></td>
<td>• Consideration transferred by the acquirer in a business combination (ASC 805-30-30-7).</td>
<td></td>
</tr>
<tr>
<td>805-40</td>
<td>• Consideration transferred in a reverse acquisition (ASC 805-40-30-2).</td>
<td></td>
</tr>
<tr>
<td>805-50</td>
<td>• Difference between the fair value and carrying amount of a noncash asset given as consideration in an asset acquired in an exchange transaction (ASC 805-50-30-1).</td>
<td>• Initial carrying amount of an asset acquired in an asset acquisition (ASC 805-50-30-2).</td>
</tr>
</tbody>
</table>

See Section 2.3.6 for discussion of exceptions to the measurement principle in ASC 805-20-30-1.
### Items That an Entity Is Required or Permitted to Recognize at Fair Value in Accordance With ASC 820

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</tr>
</thead>
<tbody>
<tr>
<td>810-10</td>
<td>• Fair value of any consideration paid, any noncontrolling interest, and the net amount of the VIE's identifiable assets and liabilities recognized under ASC 805 when the primary beneficiary of a VIE that is not a business initially consolidates the VIE (ASC 810-10-30-4). &lt;br&gt;• Assets, liabilities, and noncontrolling interests of a VIE as of the date of initial consolidation if (1) earlier consolidation was prevented because of a lack of information and (2) it is not practicable to determine carrying amounts (ASC 810-10-30-8B). &lt;br&gt;• The financial assets and financial liabilities of a CFE on the basis of the more observable of the fair value of the financial assets or the fair value of the financial liabilities (ASC 810-10-30-11 through 30-15).&lt;sup&gt;21&lt;/sup&gt; &lt;br&gt;• The financial assets and financial liabilities of a CFE if the measurement alternative is not applied (ASC 810-10-30-16). &lt;br&gt;• Consideration received and any retained noncontrolling interest when a parent deconsolidates a subsidiary or a group of assets as specified in ASC 810-10-40-3A (ASC 810-10-40-5(a)).</td>
<td>• The financial assets and financial liabilities of a CFE on the basis of the more observable of the fair value of the financial assets or the fair value of the financial liabilities (ASC 810-10-35-6 through 35-9).&lt;sup&gt;22&lt;/sup&gt;</td>
</tr>
<tr>
<td>810-30</td>
<td>• Dividend recognized for the distribution of common stock of a specified research and development arrangement (ASC 810-30-30-1).</td>
<td></td>
</tr>
</tbody>
</table>

<sup>21</sup> See Section 2.3.3 for more information about financial assets and financial liabilities of a CFE accounted for in accordance with ASC 810-10-30-11 through 30-15.

<sup>22</sup> See footnote 21.
Table continued

<table>
<thead>
<tr>
<th>ASC Subtopic</th>
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<th>Subsequent Recurring Fair Value Measurement</th>
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</thead>
<tbody>
<tr>
<td>815-10²³</td>
<td>• Derivative instruments (ASC 815-10-05-4, ASC 815-10-30-1, and ASC 815-10-30-3).²⁴</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Forward-commitment dollar rolls that do not meet the definition of a derivative (ASC 815-10-30-4).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Debt security purchased under a forward purchase contract and classified as available for sale (ASC 815-10-35-5(b)(2)).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Debt security purchased under a forward purchase contract or an option contract that is classified as trading (ASC 815-10-35-5(c)(2)).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Equity security purchased under a forward purchase contract or an option contract (ASC 815-10-35-6).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Forward purchase contract or purchased option on an equity security that (1) does not have a readily determinable fair value and is accounted for by using the practical expedient in ASC 321-10-35-2 upon the occurrence of (a) an observable price change or (b) an impairment loss or (2) was accounted for by using the practical expedient in ASC 321-10-35-2 and (a) subsequently has a readily determinable fair value or (b) is elected to be accounted for at fair value (ASC 815-10-35-6).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Derivative instruments (ASC 815-10-05-4 and ASC 815-10-35-1 through 35-1C).²⁵</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Forward-commitment dollar rolls that do not meet the definition of a derivative (ASC 815-10-35-4).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Forward purchase contract or purchased option on a debt security that is classified as available for sale (ASC 815-10-35-5(b)(1)).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Forward purchase contract or purchased option on a debt security that is classified as trading (ASC 815-10-35-5(c)(1)).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Forward purchase contract or purchased option on an equity security that (1) has a readily determinable fair value or (2) does not have a readily determinable fair value and is not accounted for by using the practical expedient in ASC 321-10-35-2 (ASC 815-10-35-6).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Option granted to an employee that becomes subject to ASC 815 (ASC 815-10-45-10).</td>
<td></td>
</tr>
</tbody>
</table>

²³ This table does not include any references to the guidance in ASC 815-20, ASC 815-25, ASC 815-30, and ASC 815-35 regarding how to recognize the change in fair value of a derivative or nonderivative instrument designated as a hedging instrument. ASC 815-10-35-2 states that “[t]he accounting for changes in the fair value (that is, gains or losses) of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship.” When ASC 815-20, ASC 815-25, ASC 815-30, or ASC 815-35 refers to “fair value” with respect to assessing, measuring, or recognizing the effects of hedge accounting, the measurement guidance in ASC 820 applies. However, depending on how fair value is used in the application of hedge accounting, a resulting measurement may not be a fair value measurement. See Section 2.3.11 for more information about the hedged item in a fair value hedge accounted for under ASC 815-25.

²⁴ Some instruments that possess the characteristics of a derivative instrument under ASC 815-10 are subject to an exception from derivative accounting, while other instruments that do not have these characteristics are nevertheless subject to derivative accounting. As discussed in ASC 815-10-15-71, a loan commitment related to the origination of mortgage loans that will be held for sale must be accounted for as a derivative instrument regardless of whether it possesses all the characteristics of a derivative instrument.

²⁵ See footnote 24.
### Items That an Entity Is Required or Permitted to Recognize at Fair Value in Accordance With ASC 820

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</thead>
</table>
| 815-15       | - Hybrid instrument (1) for which separation of an embedded derivative would otherwise be required and (2) that an entity elects to account for at fair value in its entirety (ASC 815-15-25-4 and 25-5 and ASC 815-15-30-1).<sup>26</sup>  
- Hybrid instrument for which an entity cannot reliably identify and measure the embedded derivative that must be bifurcated (ASC 815-15-25-53 and ASC 815-15-30-1).<sup>26</sup>  
- Embedded derivative that must be separated from a hybrid instrument (ASC 815-15-30-2 and 30-3).  
- Increase in equity resulting from the reclassification of a conversion option in a convertible debt instrument from an embedded derivative liability to equity (ASC 815-15-35-4).  
- Decrease in equity resulting from the extinguishment of the conversion option in a convertible debt instrument that contains a separate equity component as a result of a previous reclassification of the conversion option from an embedded derivative liability to equity (ASC 815-15-40-4). | - Hybrid instrument (1) for which separation of an embedded derivative would otherwise be required and (2) that an entity elects to account for at fair value in its entirety (ASC 815-15-25-4 and 25-5 and ASC 815-15-35-1).<sup>26</sup>  
- Hybrid instrument for which an entity cannot reliably identify and measure the embedded derivative that must be bifurcated (ASC 815-15-25-53 and ASC 815-15-35-2).<sup>26</sup>  
- Embedded derivative that must be separated from a hybrid instrument (ASC 815-15-35-2A). |
| 815-40       | - Issuer's initial measurement of an equity-linked contract (ASC 815-40-30-1).  
- Issuer's measurement of an equity-linked contract that is reclassified from equity to an asset or liability (ASC 815-40-35-9).  
- Issuer's initial measurement of put warrants (ASC 815-40-55-18). | - Issuer's subsequent measurement of an equity-linked contract that is classified as an asset or liability (ASC 815-40-35-4).  
- Issuer's subsequent measurement of put warrants (ASC 815-40-55-18). |
| 815-45       | - Weather derivatives entered into for trading or speculative activities (ASC 815-45-30-4). | - Liability for a written nonexchange-traded-option-based weather derivative (ASC 815-45-35-5).  
- Weather derivatives entered into for trading or speculative activities (ASC 815-45-35-7). |
| 825-10       | - Eligible financial assets, financial liabilities, insurance contracts, or warranty contracts for which an entity has elected the FVO (ASC 825-10-15-4 and 15-5).<sup>27</sup> | - Eligible financial assets, financial liabilities, insurance contracts, or warranty contracts for which an entity has elected the FVO (ASC 825-10-15-4 and 15-5).<sup>27</sup> |

<sup>26</sup> See Section 2.3.2 and Chapter 12 for more information about the FVO election under ASC 825.

<sup>27</sup> See footnote 26.
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<tbody>
<tr>
<td>830-20</td>
<td>• Investment in a foreign-denominated, available-for-sale debt security (ASC 830-20-35-6).</td>
<td></td>
</tr>
<tr>
<td>835-30</td>
<td>• Note receivable; sales price; and cost of property, goods, or services exchanged when interest on the note is not stated, the stated amount is unreasonable, or the stated face amount of the note materially differs from the current cash sales price (ASC 835-30-25-5 and ASC 835-30-25-10 and 25-11).</td>
<td></td>
</tr>
<tr>
<td>840-10, 840-20, 840-30, and 840-40</td>
<td>• Any fair value measurement that does not pertain to lease classification or measurement.</td>
<td></td>
</tr>
<tr>
<td>842-50</td>
<td>• Impairment loss on the residual value of a leased asset when the lessor sells substantially all of the minimum lease payments associated with a leveraged lease and retains an interest in the residual value of the asset (ASC 842-50-35-21).</td>
<td></td>
</tr>
<tr>
<td>845-10</td>
<td>• Nonmonetary transactions, including nonreciprocal transfers (ASC 845-10-30-1 through 30-4 and ASC 845-10-30-10).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Non-pro-rata split-off of a segment of a business in a corporate plan of reorganization (ASC 845-10-30-12 and 30-13).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Dividends-in-kind recognized under ASC 845-10-25-3 (ASC 845-10-30-14).</td>
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</tr>
<tr>
<td></td>
<td>• Certain purchases and sales of inventory with the same counterparty (ASC 845-10-30-15 and 30-16).</td>
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</tr>
<tr>
<td></td>
<td>• Impairment losses on barter credits (ASC 845-10-30-19).</td>
<td></td>
</tr>
<tr>
<td>852-20</td>
<td>• Assets and liabilities in certain quasi-reorganizations (ASC 852-20-05-1).</td>
<td></td>
</tr>
</tbody>
</table>

28 See Section 2.3.1 for more information about notes receivable or payable accounted for under ASC 835-30.
29 See Section 2.3.8 for more information about lease contracts accounted for under ASC 840.
30 See Section 2.3.8 for more information about lease contracts accounted for under ASC 842.
31 See Section 2.3.12 for more information about nonmonetary transactions accounted for under ASC 845-10.
### Table

<table>
<thead>
<tr>
<th>ASC Subtopic</th>
<th>Initial Measurement or Subsequent Nonrecurring Fair Value Measurement</th>
<th>Subsequent Recurring Fair Value Measurement</th>
</tr>
</thead>
<tbody>
<tr>
<td>860-20</td>
<td>• Asset obtained or liability incurred by a transferor upon completion of a transfer of financial assets that meets the conditions to be accounted for as a sale (ASC 860-20-30-1, ASC 860-20-55-21, ASC 860-20-55-24 and 55-25, and ASC 860-20-55-83). • Asset or liability recognized by a transferee upon completion of a transfer of financial assets (ASC 860-20-30-2). • Transferred financial assets and liabilities that are re-recognized by a transferor upon regaining control of financial assets (ASC 860-20-30-3).</td>
<td>• Financial assets subject to prepayment (ASC 860-20-35-2).</td>
</tr>
<tr>
<td>860-30</td>
<td>• Noncash collateral recognized by a secured party as its asset that the secured party has not already sold (ASC 860-30-30-1).</td>
<td>• Bank or savings institution that, as a transferee, sells transferred collateral and recognizes a liability for the sold collateral (ASC 860-30-35-3).</td>
</tr>
<tr>
<td>860-50</td>
<td>• Servicing assets or servicing liabilities that qualify for separate recognition (ASC 860-50-30-1). • Impairment loss on a class of servicing assets accounted for by using the amortization method (ASC 860-50-35-9(b)). • Increase in the fair value of a class of servicing liabilities accounted for by using the amortization method (ASC 860-50-35-11).</td>
<td>• Classes of servicing assets or servicing liabilities accounted for by using the fair value measurement method (ASC 860-50-35-1 and ASC 860-50-35-3(e)).</td>
</tr>
<tr>
<td>920-350</td>
<td>• Capitalized costs of rights to program materials (ASC 920-350-30-3 and ASC 920-350-35-3). • Termination of a network affiliation agreement that is replaced (ASC 920-350-40-1).</td>
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</tr>
<tr>
<td>920-405</td>
<td>• Asset and liability for a broadcast license agreement by a licensee (ASC 920-405-30-1).</td>
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</tr>
<tr>
<td>926-20</td>
<td>• Impairment losses on unamortized film costs (ASC 926-20-35-13). • Impairment losses on film properties in development (ASC 926-20-40-3).</td>
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<tbody>
<tr>
<td>932-360</td>
<td>• Impairment losses on an oil- and gas-producing property (ASC 932-360-35-8).</td>
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<tr>
<td>940-20</td>
<td>• Loss on a conditional transaction (ASC 940-20-25-7).</td>
<td>• Securities underlying amounts in suspense accounts (ASC 940-20-35-2).</td>
</tr>
<tr>
<td></td>
<td>• Fail-to-receive liabilities (ASC 940-20-30-2).</td>
<td>• Shares in an underwriting for which the underwriter is firmly committed to purchase any shares to which customers have not yet subscribed (ASC 940-20-35-3).</td>
</tr>
<tr>
<td></td>
<td>• Fair value gain deferred on a conditional transaction (ASC 940-20-35-1).</td>
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</tr>
<tr>
<td>940-320</td>
<td>• Securities from proprietary trading (ASC 940-320-30-2).</td>
<td>• Securities from proprietary trading (ASC 940-320-35-1).</td>
</tr>
<tr>
<td>940-325</td>
<td>• Investment in the form of equity or financing provided to another entity in a financial-restructuring transaction (ASC 940-325-30-1).</td>
<td>• Investment in the form of equity or financing provided to another entity in a financial-restructuring transaction (ASC 940-325-35-1).</td>
</tr>
<tr>
<td>940-340</td>
<td>• Exchange membership recognized as a contributed interest and the related subordinated liability (ASC 940-340-30-2).</td>
<td>• Exchange membership recognized as a contributed interest and the related subordinated liability (ASC 940-340-35-2).</td>
</tr>
<tr>
<td>942-310</td>
<td>• Debt-equity swaps (ASC 942-310-30-1).</td>
<td>• Obligation for a short sale (ASC 942-405-35-1).</td>
</tr>
<tr>
<td></td>
<td>• An impairment loss on a debt-equity swap (ASC 942-310-35-5)</td>
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<tr>
<td></td>
<td>• Loan receivable to be disposed of “by sale of swap” (ASC 942-310-55-1)</td>
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<tr>
<td>942-405</td>
<td></td>
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<tr>
<td>944-20</td>
<td></td>
<td>• Liability to the contract holder for a group-participating pension contract (ASC 944-20-55-12),</td>
</tr>
<tr>
<td>944-40</td>
<td>• Asset or liability for a market risk benefit (ASC 944-40-30-19C).</td>
<td>• Liability for certain group-participating pension contracts and experience-related contracts (ASC 944-40-25-19),</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Asset or liability for a market risk benefit (ASC 944-40-35-8A).</td>
</tr>
</tbody>
</table>
### Items That an Entity Is Required or Permitted to Recognize at Fair Value in Accordance With ASC 820

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<tr>
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<tr>
<td>944-80</td>
<td>• Asset and liability for the portion of separate-account assets representing contract holder funds (ASC 944-80-30-1).</td>
<td>• Asset and liability for certain investments in separate-account assets (ASC 944-80-35-1 and 35-2).</td>
</tr>
<tr>
<td></td>
<td>• Asset transferred from the general account to a separate account to the extent of third-party contract holders' proportionate interests in the separate account for certain separate-account arrangements (ASC 944-80-35-3 and ASC 944-80-40-1).</td>
<td></td>
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<td></td>
<td>• Impairment loss on an insurance entity's proportionate interest in a separate-account arrangement (ASC 944-80-35-8).</td>
<td></td>
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<tr>
<td></td>
<td>• Increase in an insurance entity's proportionate interest in a separate-account arrangement as a result of a transaction executed at fair value (ASC 944-80-35-10).</td>
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</tr>
<tr>
<td>944-360</td>
<td>• Real estate acquired in settling mortgage guaranty and title insurance claims (ASC 944-360-30-1).</td>
<td></td>
</tr>
<tr>
<td>944-805</td>
<td>• Asset or liability recognized by an acquirer for insurance and reinsurance contracts obtained in a business combination (ASC 944-805-30-1).</td>
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</tr>
<tr>
<td>944-815</td>
<td></td>
<td>• Liability for a traditional variable annuity contract that is based on the fair value of the assets held in a separate account for policyholders (ASC 944-815-25-2).</td>
</tr>
<tr>
<td>946-10</td>
<td>• Initial carrying amount of an investment as of the date on which an entity is no longer an investment company (ASC 946-10-25-2).</td>
<td></td>
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<tr>
<td></td>
<td>• Adjustment to net assets for the difference between the carrying amount and fair value of an investment as of the date on which an entity becomes an investment company (ASC 946-10-25-3).</td>
<td></td>
</tr>
<tr>
<td>946-320</td>
<td>• Stock dividends (ASC 946-320-35-6).</td>
<td>• Investment in a debt or equity security (ASC 946-320-35-1).</td>
</tr>
<tr>
<td></td>
<td>• Other noncash dividends (ASC 946-320-35-7).</td>
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<tr>
<td>946-325</td>
<td></td>
<td>• Other investments (ASC 946-325-35-1).</td>
</tr>
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</tbody>
</table>
| 946-830      | • Forward exchange contracts (ASC 946-830-05-2(e) and ASC 946-830-45-10).  
              • Purchased interest (i.e., interest accrued between the last coupon date and the settlement date of the purchase) (ASC 946-830-45-14). |                                            |
| 948-310      | • Mortgage loan to be sold to an affiliated entity (ASC 948-310-30-1).  
              • Mortgage loan held for sale (ASC 948-310-35-1).  
              • Mortgage loan transferred to a long-term investment classification (ASC 948-310-30-4). |                                            |
| 950-350      | • Consideration paid to purchase a title plant (ASC 950-350-30-2). |                                            |
| 958-30       | • Embedded derivative related to certain split-interest agreements (ASC 958-30-25-12, ASC 958-30-25-14, ASC 958-30-30-9, ASC 958-30-55-10, and ASC 958-30-55-23).  
              • Liability recognized for certain split-interest agreements (ASC 958-30-25-10 and ASC 958-30-30-5).  
              • Asset received by an NFP entity acting as a trustee under a revocable split-interest agreement (ASC 958-30-30-3).  
              • Asset that is received by an NFP entity acting as a trustee or that is otherwise under the control of the NFP entity as part of an irrevocable split-interest agreement (ASC 958-30-30-4).  
              • Contributed asset received from a donor under a pooled income fund agreement or net income unitrust (ASC 958-30-30-10).  
              • Beneficial interest in a split-interest agreement of a third party that is owned by an NFP entity (ASC 958-30-30-11).  
              • Embedded derivative related to certain split-interest agreements (ASC 958-30-25-12, ASC 958-30-25-14, ASC 958-30-35-7, ASC 958-30-55-10, and ASC 958-30-55-23).  
              • Liability recognized for certain split-interest agreements (ASC 958-30-35-2 and ASC 958-30-35-8).  
              • Beneficial interest in a split-interest agreement of a third party that is owned by an NFP entity (ASC 958-30-35-10). |                                            |
| 958-310      | • Changes in a contribution receivable arising from an unconditional promise to give debt securities or equity securities with readily determinable fair values (ASC 958-310-35-11).  
              • Changes in a contribution receivable arising from a promise to give noncash assets (ASC 958-310-35-13). |                                            |
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<tr>
<td>958-320</td>
<td>• Investment in a debt security received as a contribution or through an agency transaction (ASC 958-320-30-1).</td>
<td>• Investments in debt securities (ASC 958-320-35-1).</td>
</tr>
<tr>
<td>958-321</td>
<td>• Investment in an equity security received as a contribution or through an agency transaction (ASC 958-321-30-1).</td>
<td>• Investment in an equity security that must be measured at fair value under ASC 321 (ASC 958-321-35-1).</td>
</tr>
<tr>
<td>958-325</td>
<td>• Other investments received as a contribution or through an agency transaction (ASC 958-325-30-1). • Impairment losses on other investments measured at carrying value by a voluntary health and welfare entity (ASC 958-325-35-5). • Impairment losses on other investments measured at the lower of cost or fair value by an NFP entity that is not a college, university, voluntary health and welfare, or health care entity (ASC 958-325-35-7).</td>
<td>• Other investments measured at fair value by an institution of higher education, including a college, university, and community or junior college (ASC 958-325-35-1). • Other investments measured at fair value by a voluntary health and welfare entity (ASC 958-325-35-3). • Other investments measured at fair value by an NFP entity that is not a college, university, voluntary health and welfare, or health care entity (ASC 958-325-35-6).</td>
</tr>
<tr>
<td>958-360</td>
<td>• Contribution of a recognized collection item made by an NFP entity (ASC 958-360-40-2).</td>
<td>• Asset for a beneficial interest that entitles the holder of an unconditional right to receive all or a portion of the specified cash flows from a charitable trust or other identifiable pool of assets (ASC 958-605-35-3).</td>
</tr>
</tbody>
</table>
| 958-605      | • Direct personnel costs incurred by an affiliate that provides a service to an NFP entity (ASC 958-605-25-17). • Gift in kind reported as a contribution when originally received by an NFP entity (ASC 958-605-25-20 and ASC 958-605-30-11). • Contribution received by an NFP entity (ASC 958-605-30-2 and ASC 958-695-30-7). • Asset and liability of an intermediary that raises or holds contributions for others (ASC 958-605-30-12). • Asset and liability of an agent that raises or holds contributions for others (ASC 958-605-30-13). • Asset for a beneficial interest that entitles the holder with an unconditional right to receive all or a portion of the specified cash flows from a charitable trust or another identifiable pool of assets (ASC 958-605-30-14). | See Section 2.3.18 for more information about contributions accounted for under ASC 958-605. See footnote 32.
(Table continued)

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<tr>
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</table>
| 958-720      | • Liability and expense for an unconditional promise to give (ASC 958-720-30-1).  
               • Services received from personnel of an affiliate that directly benefit the recipient NFP entity (ASC 958-720-30-3). |                                           |
| 958-805      | • Gains and losses for the difference between the carrying amount and fair value of consideration transferred (ASC 958-805-25-34 and ASC 958-805-30-11).  
               • Identifiable assets acquired, liabilities assumed, and any noncontrolling interest in an acquiree in an acquisition by an NFP entity in accordance with ASC 805-20 (ASC 958-805-30-5).  
               • Consideration transferred in an acquisition by an NFP entity that is a business combination, including contingent consideration (ASC 958-805-30-10 and ASC 958-805-30-13). | • Asset or liability for contingent consideration (ASC 958-805-35-3). |
| 958-810      | • Certain investments of NFP entities that are not health care entities within the scope of ASC 954 (ASC 958-810-15-4). |                                           |
| 960-30       | • Noncash contribution from an employer (ASC 960-30-45-2(c)). |                                           |
| 960-325      | • Plan investments other than insurance contracts reported at contract value (ASC 960-325-35-1 through 35-3).  
               • Plan investments other than FBRICs (ASC 962-325-35-1 and 35-1A and ASC 962-325-35-5 and 35-6).  
               • Plan investments in the form of equity or debt securities (ASC 965-320-35-1). |                                           |
| 965-20       | • Noncash contributions (ASC 965-20-30-1). |                                           |

34 See Section 2.3.16 for more information about plan assets and obligations accounted for under ASC 960-325.  
35 See Section 2.3.16 for more information about plan assets and obligations accounted for under ASC 962-325.  
36 See Section 2.3.16 for more information about the accounting for plan assets and obligations under ASC 965-320.
2.1.3 Disclosure

ASC 820's disclosure requirements do not apply to fair value measurements at initial recognition (i.e., to initial measurements of assets, liabilities, equity instruments, or transactions at fair value). 37 However, with certain exceptions, assets and liabilities that are subsequently measured at fair value on a recurring or nonrecurring basis in accordance with ASC 820 are subject to ASC 820's disclosure requirements (see Section 2.3 for more information). In addition, ASC 820 requires entities to disclose fair value amounts measured in accordance with ASC 820 as well as other fair-value-related information for certain assets and liabilities that are not measured at fair value. 40 Other Codification topics also require certain disclosures regarding fair value amounts, including when an asset, liability, equity instrument, or transaction is initially measured at fair value. In these circumstances, in the absence of a specific scope exception in ASC 820 or another Codification topic, the fair value information must be prepared on the basis of the measurement guidance in ASC 820.

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37 See Section 2.3.16 for more information about the accounting for plan assets and obligations under ASC 965-325.
38 See Section 2.3.16 for more information about the accounting for plan assets and obligations under ASC 965-360.
39 Items initially measured on the basis of a relative fair value allocation are also not subject to ASC 820’s disclosure requirements.
40 Under ASC 820-10-50-2E, certain disclosure provisions of ASC 820 apply to classes of “assets and liabilities not measured at fair value in the statement of financial position but for which the fair value is disclosed,” including financial instruments for which fair value is disclosed under ASC 825. These disclosure requirements have been incorporated into ASC 825-10-50-10 through 50-15.
See Chapter 11 for more information about the fair value disclosure requirements in ASC 820. See Appendix A for more information about other Codification topics that require fair value disclosures.

Connecting the Dots

Entities in certain industries, such as real estate, may prepare basic financial statements under U.S. GAAP and report fair value information as a supplement to the financial statements. Other entities may disclose fair value amounts related to particular assets, liabilities, and equity instruments. ASC 820 applies to the disclosure of such supplemental fair value information. ASC 820-10-15-1 states that the guidance in ASC 820 “applies when another Topic requires or permits fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements).”

2.2 Practicability Exceptions

2.2.1 General

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Practicability Exceptions to This Topic

15-3 The Fair Value Measurement Topic does not eliminate the practicability exceptions to fair value measurements within the scope of this Topic. Those practicability exceptions to fair value measurements in specified circumstances include, among others, those stated in the following:

a. The use of a transaction price (an entry price) to measure fair value (an exit price) at initial recognition, including the following:
   1. Guarantees in accordance with Topic 460
   2. Subparagraph superseded by Accounting Standards Update No. 2009-16
b. Subparagraph superseded by Accounting Standards Update No. 2016-01
   1. Subparagraph superseded by Accounting Standards Update No. 2016-01
   2. Subparagraph superseded by Accounting Standards Update No. 2009-16
c. An exemption to the requirement to measure fair value if fair value is not reasonably determinable, such as all of the following:
   1. Nonmonetary assets in accordance with Topic 845 and Sections 605-20-25 and 605-20-50
   2. Asset retirement obligations in accordance with Subtopic 410-20 and Sections 440-10-50 and 440-10-55
   3. Restructuring obligations in accordance with Topic 420
   4. Participation rights in accordance with Subtopics 715-30 and 715-60.
d. Subparagraph superseded by Accounting Standards Update No. 2015-10
e. The use of particular measurement methods referred to in paragraph 805-20-30-10 that allow measurements other than fair value for specified assets acquired and liabilities assumed in a business combination.
ee. Financial assets or financial liabilities of a consolidated variable interest entity that is a collateralized financing entity when the financial assets or financial liabilities are measured using the measurement alternative in paragraphs 810-10-30-10 through 30-15 and 810-10-35-6 through 35-8.
f. An exemption to the requirement to measure fair value if fair value cannot be reasonably estimated, such as the following:
   1. Noncash consideration promised in a contract in accordance with the guidance in paragraphs 606-10-32-21 through 32-24.
ASC 820-10-15-3 discusses various practicability exceptions that allow entities to recognize certain items at amounts other than fair value. These practical expedients merely acknowledge the measurement exceptions provided in other Codification topics. See Section 2.3 for further discussion of these practical expedients.

2.2.2 Certain Entities That Calculate NAV per Share (or Its Equivalent)

ASC 820-10

**Fair Value Measurements of Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)**

15-4 Paragraphs 820-10-35-59 through 35-62 and 820-10-50-6A shall apply only to an investment that meets both of the following criteria as of the reporting entity’s measurement date:

a. The investment does not have a readily determinable fair value
b. The investment is in an investment company within the scope of Topic 946 or is an investment in a real estate fund for which it is industry practice to measure investment assets at fair value on a recurring basis and to issue financial statements that are consistent with the measurement principles in Topic 946.

15-5 The definition of **readily determinable fair value** indicates that an equity security would have a readily determinable fair value if any one of three conditions is met. One of those conditions is that sales prices or bid-and-asked quotations are currently available on a securities exchange registered with the U.S. Securities and Exchange Commission (SEC) or in the over-the-counter market, provided that those prices or quotations for the over-the-counter market are publicly reported by the National Association of Securities Dealers Automated Quotations systems or by OTC Markets Group Inc. The definition notes that restricted stock meets that definition if the restriction expires within one year. If an investment otherwise would have a readily determinable fair value, except that the investment has a restriction expiring in more than one year, the reporting entity shall not apply paragraphs 820-10-35-59 through 35-62 and 820-10-50-6A to the investment.

**Measuring the Fair Value of Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)**

35-59 A reporting entity is permitted, as a practical expedient, to estimate the fair value of an investment within the scope of paragraphs 820-10-15-4 through 15-5 using the net asset value per share (or its equivalent, such as member units or an ownership interest in partners’ capital to which a proportionate share of net assets is attributed) of the investment, if the net asset value per share of the investment (or its equivalent) is calculated in a manner consistent with the measurement principles of Topic 946 as of the reporting entity’s measurement date.

35-60 If the net asset value per share of the investment obtained from the investee is not as of the reporting entity’s measurement date or is not calculated in a manner consistent with the measurement principles of Topic 946, the reporting entity shall consider whether an adjustment to the most recent net asset value per share is necessary. The objective of any adjustment is to estimate a net asset value per share for the investment that is calculated in a manner consistent with the measurement principles of Topic 946 as of the reporting entity’s measurement date.

35-61 A reporting entity shall decide on an investment-by-investment basis whether to apply the practical expedient in paragraph 820-10-35-59 and shall apply that practical expedient consistently to the fair value measurement of the reporting entity’s entire position in a particular investment, unless it is probable at the measurement date that the reporting entity will sell a portion of an investment at an amount different from net asset value per share (or its equivalent) as described in the following paragraph. In those situations, the reporting entity shall account for the portion of the investment that is being sold in accordance with this Topic (that is, the reporting entity shall not apply the guidance in paragraph 820-10-35-59).
ASC 820-10 (continued)

35-62 A reporting entity is not permitted to estimate the fair value of an investment (or a portion of the investment) within the scope of paragraphs 820-10-15-4 through 15-5 using the net asset value per share of the investment (or its equivalent) as a practical expedient if, as of the reporting entity's measurement date, it is probable that the reporting entity will sell the investment for an amount different from the net asset value per share (or its equivalent). A sale is considered probable only if all of the following criteria have been met as of the reporting entity's measurement date:

a. Management, having the authority to approve the action, commits to a plan to sell the investment.

b. An active program to locate a buyer and other actions required to complete the plan to sell the investment have been initiated.

c. The investment is available for immediate sale subject only to terms that are usual and customary for sales of such investments (for example, a requirement to obtain approval of the sale from the investee or a buyer's due diligence procedures).

d. Actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

The scoping conditions in ASC 810-20-15-4 and 15-5 allow certain entities, as a practical expedient, to estimate the fair value of certain investments that do not have a readily determinable fair value at NAV per share (or its equivalent). As noted in ASC 820-10-35-61, the decision of whether to apply this practical expedient is made on an investment-by-investment basis. An entity that chooses to use this practical expedient must apply it consistently to the fair value measurement of the entity's entire position in a particular investment, unless it is probable as of the measurement date that the entity will sell a portion of the investment at an amount different from NAV value per share (or its equivalent), in which case use of the practical expedient is not permitted.

ASC 820-10-35-62 indicates that, for a sale of an investment to be probable, four criteria must be met as of the measurement date. For these four criteria to be met, the entity must identify the individual investment(s) to be sold. That is, if the entity decides to sell a portion of a group of assets (e.g., 25 percent of the total group) but has not identified the individual investments to be sold, the entity could not conclude that it is probable that any individual investment will be sold.

An entity must often use significant judgment in evaluating whether a sale for an amount different from NAV per share (or its equivalent) is considered probable and should establish consistent processes and documentation protocols for evaluating and supporting its conclusions, including the probability assertion based on the four criteria in ASC 820-10-35-62. Management should carefully assess any changes in assertions. For example, a change in assertion that results in the triggering of significant profits (or losses) in a particular period could call into question the primary intent of the change and the validity of the entity's assertion.

If an entity subsequently determines that it is no longer probable that the reporting entity will sell the investment for an amount different from NAV per share (or its equivalent) (i.e., the criteria in ASC 820-10-35-62 are no longer met), the entity is permitted to use NAV as a practical expedient in measuring the fair value of the investment provided that the investment continues to be within the scope of ASC 820-10-15-4 and 15-5. This conclusion is consistent with informal discussions with the FASB staff.

See Sections 10.9, 11.2.2.3, and 11.3.2.3 for further discussion of the NAV practical expedient.
2.2.3 Mid-Market and Other Pricing Conventions

ASC 820-10-35-36D states that “[ASC 820] does not preclude the use of mid-market pricing or other pricing conventions that are used by market participants as a practical expedient for fair value measurements within a bid-ask spread.” See Section 10.4.4 for more information.

2.2.4 Simplified Hedge Accounting Approach

ASC 815-10-35-1A contains a practical expedient related to the requirement in ASC 815-10-35-1 to measure all derivative assets and liabilities at fair value. Under the practical expedient, a receive-variable, pay-fixed interest rate swap to which an entity applies the simplified method of hedge accounting in ASC 815-20-25-131AB through 25-131E “may be measured subsequently at settlement value instead of fair value.” ASC 815-10-35-1B states that “[t]he primary difference between settlement value and fair value is that nonperformance risk is not considered in determining settlement value.” ASC 815-10-35-1C clarifies that “[i]f any of the conditions . . . for applying the simplified hedge accounting approach subsequently cease to be met or the relationship otherwise ceases to qualify for hedge accounting,” the interest rate swap must be recognized at fair value both as of the date of the change and prospectively.

2.3 Application of ASC 820 to Specific Assets, Liabilities, and Equity Instruments

2.3.1 Notes Receivable and Notes Payable

2.3.1.1 Measurement

ASC 835-30 addresses the imputation of interest on notes receivable and notes payable. At initial recognition, an entity is required to calculate the appropriate discount or premium so that interest income or expense on the note receivable or note payable can be appropriately recognized in accordance with the interest method. When a note receivable or note payable is initially recognized on the basis of a present value technique (i.e., present value is used to initially recognize the note receivable or payable), the measurement is a fair value measurement. The discount rate used in the initial measurement (e.g., the rate commensurate with the risk) embodies the same notion as the discount rate used in the traditional approach (or the discount rate adjustment technique) described in FASB Concepts Statement 7 and clarified in ASC 820. Accordingly, the guidance in ASC 820-10-55-4 through 55-20 and ASC 820-10-55-33 and 55-34 on using present value techniques to measure fair value applies to initial measurements required under ASC 835-30 as well as to similar measurements required under other Codification topics.

The fair value measurement guidance in ASC 820 applies to the subsequent measurement of a note receivable or note payable only if (1) it is subsequently measured at fair value on a recurring basis in accordance with the FVO in ASC 825 or another Codification topic or (2) an impairment loss or recovery is recognized for a note receivable on the basis of a fair value measurement (i.e., a nonrecurring fair value measurement).

Connecting the Dots

An impairment loss may be recognized for an individual note or loan receivable on the basis of a present value calculation in accordance with ASC 310-10 or ASC 326-20. In this circumstance, the measurement attribute of the impaired note or loan receivable is the present value of expected future cash flows discounted at the instrument's original effective interest rate. This is not a fair value measurement because a fair value measurement would incorporate the current market discount rate. However, if impairment is measured on the basis of a practical expedient, such as the fair value of the underlying collateral or, for entities that have not yet adopted ASU
2016-13, the loan’s observable market price, the fair value measurement guidance in ASC 820 does apply. Thus, the measurement and disclosure provisions of ASC 820 do not apply to a present value measurement but do apply to a measurement that is based on an observable market price or the related collateral’s fair value (even if the impairment is recognized on the basis of the fair value of collateral, less costs to sell).

2.3.1.2 Disclosure
ASC 820’s disclosure requirements do not apply to fair value measurements at initial recognition. Therefore, the initial measurement of notes receivable or payable on the basis of a present value technique is not subject to the disclosure requirements of ASC 820. ASC 820’s disclosure requirements related to subsequent measurement would apply only if (1) a note receivable or note payable is subsequently measured at fair value on a recurring basis in accordance with the FVO in ASC 825 or another Codification topic or (2) an impairment loss or recovery is recognized for a note receivable on the basis of a fair value measurement (i.e., a nonrecurring fair value measurement). The fair value disclosures required by ASC 825-10-50-10 through 50-15 apply to notes receivable and notes payable, which are financial instruments.

2.3.2 Certain Financial Instruments
2.3.2.1 Measurement
2.3.2.1.1 Financial Instruments for Which the FVO Has Been Elected
ASC 825 allows entities to irrevocably elect to account for some financial assets and financial liabilities at fair value, with changes in fair value reported in earnings or OCI (i.e., the FVO).\textsuperscript{41} The measurement guidance in ASC 820 applies to such fair value measurements. See Chapter 12 for more information about the FVO.

2.3.2.1.2 Equity Securities Without Readily Determinable Fair Values
Under ASC 321-10-35-2, entities can elect to measure equity securities without readily determinable fair values at “cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer.” When the investment is determined to be impaired on the basis of a qualitative assessment, entities that have made the election in ASC 321-10-35-2 must remeasure such equity securities at fair value in accordance with ASC 820. ASC 321-10-55-9 further indicates that the adjustments to the carrying value of an equity security without a readily determinable fair value should “reflect the fair value of the security as of the date that the observable transaction for the similar security took place.”\textsuperscript{42}

ASU 2019-04 clarifies the guidance in ASC 321-10-35-2 on remeasuring equity securities without readily determinable fair values in response to observable price changes in orderly transactions. Specifically, the ASU amends ASC 321-10-35-2 to indicate that such transactions give rise to an adjustment to the carrying amount of the equity security and that this adjustment represents an ASC 820 fair value measurement as of the date of the observable price change. Thus, regardless of whether the observable price arises from a transaction involving the identical or a similar security, that adjustment reflects a fair value measurement under ASC 820. Thus, any adjustment to the carrying amount of an equity security that is accounted for under the measurement alternative in ASC 321-10-35-2 represents a fair value measurement under ASC 820.\textsuperscript{42}

\textsuperscript{41} ASC 825-10-45-5 through 45-7 address the requirement to present separately, in OCI, the portion of the total change in fair value of a liability that results from a change in the instrument-specific credit risk.

\textsuperscript{42} On the basis of discussions with the FASB staff, we believe that this clarification from ASU 2019-04 was also applicable before the ASU’s issuance. This view is consistent with the discussion in the summary section of ASU 2016-01 as well as paragraphs BCS8(b) and BC142 of ASU 2016-01.
In paragraph BC112 of ASU 2019-04, the FASB addresses how to measure the fair value change under ASC 321-10-35-2 that arises from an observable price involving the identical or a similar security:

The Board believed that, in most cases, the observable price change in an orderly transaction of the identical or similar investment of the same issuer would generally represent the fair value change in that investment. The Board intended a consistent remeasurement at fair value for investments accounted for under the measurement alternative upon identifying (a) an orderly transaction of the identical or similar investment of the same issuer, (b) an orderly transaction of a similar investment of the same issuer, and (c) impairment. Therefore, the Board intended to require a nonrecurring fair value measurement in accordance with Topic 820 upon the occurrence and identification of any remeasurement event described in Topic 321 for equity securities without readily determinable fair value accounted for under the measurement alternative.

See Section 10.10.2 for further discussion of fair value measurements related to observable price changes.

### 2.3.2.2 Disclosure

#### 2.3.2.2.1 Disclosures About Financial Instruments Under ASC 825

ASC 825 requires certain fair value disclosures about financial instruments, including disclosures related to (1) financial instruments measured at fair value on a recurring basis under the FVO or another Codification topic and (2) certain financial instruments that are not measured at fair value on a recurring basis. As discussed in Sections 11.2.2 and 11.3.2, there are exceptions to these disclosure requirements for certain financial instruments and the fair value disclosure requirements for financial instruments that are not measured at fair value on a recurring basis apply only to public business entities. The measurement guidance in ASC 820 applies to all fair value measurements of financial instruments that are disclosed under ASC 825. For example, an entity that is disclosing the fair value of a financial liability under ASC 825 must incorporate the instrument's nonperformance risk (i.e., the effect of the entity's own credit standing, taking into account, when appropriate, any credit enhancements related to the liability) in accordance with ASC 820-10-35-17 and 35-18.

#### 2.3.2.2.2 Cash Equivalents

The disclosure requirements for cash equivalents under ASC 820 and ASC 825 depend on whether the cash equivalents are reported at fair value in the statement of financial position.

##### 2.3.2.2.2.1 Cash Equivalents Measured at Fair Value

If a cash equivalent is measured at fair value in the statement of financial position, an entity should provide all of the ASC 820 disclosures required for assets measured at fair value on a recurring basis as well as the financial instrument disclosures required by ASC 825. For example, assume that an entity has an investment in a debt security that meets the definition of a cash equivalent and is presented as such in accordance with ASC 320-10-45-13. If the debt security is classified as trading under ASC 320, it is recognized at fair value in the statement of financial position. Therefore, in such cases, the entity would classify the debt security within the ASC 820 fair value hierarchy and provide the related fair value disclosures for recurring fair value measurements reported in the statement of financial position. See Chapter 11 for more information.

##### 2.3.2.2.2 Cash Equivalents Measured at Amortized Cost

If a cash equivalent is measured at amortized cost in the statement of financial position, an entity is only required to provide the ASC 825 disclosures for financial instruments that are not measured at fair value (if applicable). For example, assume that an entity invests in a traditional CD from a bank (i.e., not a “brokered CD”) and that the CD's original maturity is 60 days. The CD does not meet the definition of a
security and therefore is not within the scope of ASC 320.⁴³ The entity has determined that it will present the CD in cash equivalents in the statement of financial position, at amortized cost, in accordance with the definition of cash equivalents and ASC 320-10-45-13. However, the CD is a financial instrument; therefore, the disclosure requirements in ASC 825-10-50-10 apply to the CD held as a cash equivalent. For more information about the applicability of the disclosure requirements in ASC 825, see Sections 11.2.2.2 and 11.3.2.2.

### 2.3.2.2.3 Equity Securities Without Readily Determinable Fair Values

As discussed in Section 2.3.2.1.2, an adjustment to the carrying amount of an equity security that is accounted for by using the measurement alternative under ASC 321-10-35-2, regardless of whether the adjustment is related to an observable price change or an impairment, represents a fair value measurement under ASC 820. Therefore, the nonrecurring disclosure requirements of ASC 820 are applicable during any financial reporting period for which such an adjustment is recognized. However, ASC 825's disclosure requirements related to financial instruments that are not measured at fair value do not apply to equity securities that are accounted for by using the measurement alternative under ASC 321-10-35-2.

### 2.3.2.2.4 Equity Method Investments

An entity does not need to provide the fair value disclosures required by ASC 820 or ASC 825 for an equity method investment accounted for under ASC 323. However, if the investment is recognized at fair value through earnings in accordance with the ASC 825 FVO or as a result of the application of specialized accounting guidance (e.g., ASC 946), an entity must provide all relevant fair value disclosures in ASC 820 that pertain to items measured at fair value on a recurring basis.⁴⁴ In addition, if an equity method investment recognized under ASC 323 is other-than-temporarily impaired (resulting in a write-down to fair value), the entity must provide all relevant ASC 820 fair value disclosures pertaining to items measured at fair value on a nonrecurring basis.

While the ASC 820 and ASC 825 fair value disclosures are not required for equity method investments recognized under ASC 323 that have not been written down to fair value as a result of an other-than-temporary impairment, an entity can voluntarily provide these disclosures for investments accounted for under the equity method. One purpose of providing such disclosures may be to give a more complete picture of the investment's value.

An entity that elects to provide fair value disclosures for equity method investments should apply a rational and consistent policy of doing so (e.g., across reporting periods and across investment types). Further, an entity that elects to present fair value disclosures for certain equity method investments should consider presenting these disclosures for all other similar investments. The entity should also (1) ensure that its disclosures clearly indicate that such equity method investments for which fair value is voluntarily disclosed are not recognized at fair value on a recurring basis in the statement of financial position and (2) separately identify the associated carrying amounts reported in the statement of financial position. This is especially important when an entity has equity method investments of a similar type and some but not all of those investments are recognized at fair value in the statement of financial position. For example, if an entity has multiple equity method investments, some but not all of which are measured at fair value on a recurring basis, the entity should disclose the fair value of the investments accounted for under the equity method (along with the associated carrying amounts) separately from the fair value of the investments that are recorded at fair value on a recurring basis.

⁴³ Certain CDs (e.g., brokered CDs) may meet the definition of a security and therefore may be within the scope of ASC 320. Accordingly, an entity must evaluate the specific terms of a CD.

⁴⁴ See Section 12.5.3.2 for discussion of the disclosures that an entity must provide under ASC 323 when electing the FVO for an investment that would otherwise be accounted for under the equity method.
The application of the disclosure requirements in ASC 820 and ASC 825 to equity method investments is further discussed below.

2.3.2.2.4.1 ASC 820 Disclosures

The guidance in ASC 820-10-15-1 applies when another Codification topic requires or permits “fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements).” Since ASC 825 permits disclosure of the fair value of investments accounted for under the equity method, an entity can also provide ASC 820 disclosures for such investments. (See Section 2.1.3 for additional guidance on applying the provisions of ASC 820 to ASC 825 disclosures.) An entity that chooses to disclose the fair value of an equity method investment may disclose the following information related to the fair value measurement (see ASC 820-10-50-2E):

- The valuation’s level in the fair value hierarchy.
- A description of the valuation technique and inputs used in the fair value measurement.

2.3.2.2.4.2 ASC 825 Disclosures

ASC 825-10-50-8(g) exempts entities from the fair value disclosure requirements related to “investments accounted for under the equity method” because ASC 323-10-50-3(b) already requires disclosure of the quoted market price of such investments when it is available. Paragraph 75 of the Background Information and Basis for Conclusions of FASB Statement 107 (superseded) addressed this issue, stating that the “incremental benefits of estimating fair value for unquoted investments accounted for under the equity method do not outweigh the related costs” of determining those fair values. However, ASC 825 does not prohibit an entity from disclosing the fair value of an investment accounted for under the equity method (i.e., from providing the disclosures discussed in ASC 825-10-50-10).

2.3.2.2.5 Investments of Feeder Funds

Many investment companies adopt complex capital structures to increase pricing flexibility as well as access to alternative distribution channels for their shares. Master-feeder structures permit distribution of a common investment vehicle (1) through different channels, (2) with different distribution charges to the shareholder, or (3) both. In such structures, the investment companies that perform the investment management function are often separate from those that perform the distribution function. Feeder investment companies have similar investment objectives but different distribution channels for their shares (such as retail or institutional customers) and invest substantially all of their assets in another investment company, known as the master fund. Investment management functions are conducted by the master fund, whereas distribution, shareholder-serving, and transfer agent functions are conducted by the feeder funds.

ASC 946-235-50-3 specifies the information a feeder fund is required to include in its financial statement notes. A feeder fund’s stand-alone financial statements generally do not have to include ASC 820 fair value disclosures, including fair value hierarchy classification and presentation of the rollforward of Level 3 assets, provided that the feeder fund invests solely in the master fund and has no other direct investments. Registered investment companies that have entered into master-feeder arrangements (as defined by the SEC) must provide the master fund’s financial statements, along with those of each feeder fund, in accordance with SEC requirements. Nonregistered investment companies should

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45 The AICPA Audit and Accounting Guide Investment Companies defines a master-feeder arrangement as “one in which a registered investment company that invests in a single investment vehicle.” Master-feeder structures are specifically permitted by Section 12(d)(1)(E)(ii) of the Investment Company Act of 1940.

46 See the SEC’s December 30, 1998, “Annual Industry Comment Letter From the Division of Investment Management.”
attach the financial statements of the master fund to those of the feeder fund. Therefore, as long as the feeder fund's disclosures refer to the fair value disclosures in the master fund's provided or attached financial statements, a feeder fund would not have to comply with ASC 820's disclosure requirements.

However, in some circumstances, a feeder fund maintains direct investments in addition to its investment in the master fund (e.g., an interest rate swap). In such cases, the feeder fund would be required to include in its financial statements the appropriate ASC 820 disclosures for those direct investments.

2.3.3 Collateralized Financing Entities

2.3.3.1 Measurement

ASC 820-10-15-3(ee) contains a practicability exception related to the initial and subsequent measurement of “[f]inancial assets or financial liabilities of a consolidated [VIE] that is a collateralized financing entity when the financial assets or financial liabilities are measured using the measurement alternative in paragraphs 810-10-30-10 through 30-15 and 810-10-35-6 through 35-8.” When a CFE meets the scope requirements in ASC 810-10-15-17D and this measurement alternative is elected, the reporting entity measures both the financial assets and the financial liabilities of the CFE by using the more observable of the fair value of the financial assets or the fair value of the financial liabilities. The fair value measurement guidance in ASC 820 applies to the more observable of the fair value of the financial assets or the fair value of the financial liabilities. See Section 8.1.2 for further discussion of this practicability exception.

2.3.3.2 Disclosure

ASC 810-10-50-20 through 50-22 address the disclosures an entity is required to provide when the measurement alternative in ASC 810-10-30-10 through 30-15 and ASC 810-10-35-6 through 35-8 is applied to a CFE. For instance, ASC 810-10-50-20 indicates that the entity “shall disclose the information required by Topic 820 on fair value measurement and Topic 825 on financial instruments for the financial assets and the financial liabilities of the consolidated collateralized financing entity.” Further, ASC 810-10-50-21 states that “[f]or the less observable of the fair value of the financial assets and the fair value of the financial liabilities of the collateralized financing entity that is measured in accordance with the measurement alternative in paragraphs 810-10-30-10 through 30-15 and 810-10-35-6 through 35-8, a reporting entity shall disclose that the amount was measured on the basis of the more observable of the fair value of the financial assets and the fair value of the financial assets.” See Section A.19 for further discussion of the disclosures an entity is required to provide when applying this practicability exception.

2.3.4 Guarantees

2.3.4.1 Measurement

The objective of initially measuring a guarantee liability under ASC 460-10 is to determine the fair value of the guarantee at its inception. However, ASC 460-10-30-2(a) and 30-2(b) state:

a. If a guarantee is issued in a standalone arm's-length transaction with an unrelated party, the liability recognized at the inception of the guarantee shall be the premium received or receivable by the guarantor as a practical expedient.

b. If a guarantee is issued as part of a transaction with multiple elements with an unrelated party (such as in conjunction with selling an asset or entering into an operating lease), the liability recognized at the inception of the guarantee should be an estimate of the guarantee's fair value. In that circumstance, a guarantor shall consider what premium would be required by the guarantor to issue the same guarantee in a standalone arm's-length transaction with an unrelated party as a practical expedient.
The recognition of a guarantee liability on the basis of the premium received or receivable represents a practical expedient because this amount reflects an entry price rather than an exit price. This practical expedient is acknowledged in ASC 820-10-15-3(a)(1).

Read literally, ASC 460-10-30-2(a) and 30-2(b) require an entity to initially recognize the guarantee liability on the basis of an entry price. However, in discussions, the FASB staff has indicated that the use of the entry price in the initial measurement of a guarantee liability is only intended to be an accommodation. Therefore, although the language may imply that an entity is required to perform initial recognition on the basis of the transaction price, the entity is not precluded from initially recognizing the guarantee liability at fair value in such circumstances (i.e., on the basis of an exit price).

See Section 10.10.9 for further discussion of the fair value measurement of guarantees.

2.3.4.2 Disclosure

ASC 820's disclosure requirements do not apply to fair value measurements at initial recognition. Therefore, the initial measurement of the liability for a guarantee obligation is not subject to these requirements. However, the fair value disclosures required by ASC 825-10-50-10 through 50-15 would be applicable. In addition, the disclosure requirements in ASC 460-10 apply to guarantees. See Section A.12 for further discussion of fair value disclosures related to guarantees.

2.3.5 Share-Based Payments

2.3.5.1 Measurement

As discussed in ASC 820-10-15-2, the guidance in ASC 820 does not apply to measurements of share-based payment awards in accordance with ASC 718 (or ASC 505-50 for entities that have not adopted ASU 2018-07). Measurements under ASC 718 (or ASC 505-50) are “fair-value-based” measurements. Valuation techniques and certain assumptions used in a fair-value-based measurement in accordance with ASC 718 (or ASC 505-50) may be consistent with those used in a fair value measurement under ASC 820. However, a fair-value-based measurement excludes the impact of certain conditions, restrictions, and contingencies that a fair value measurement under ASC 820 would include (e.g., service conditions, performance conditions and other restrictions that apply during the vesting period, reload features, and contingent features that may require the employee to return equity instruments). Under ASC 718 (and ASC 505-50), the effect of such items is taken into account not in the fair-value-based measurement but through the recognition of compensation cost only for awards for which the requisite service (or goods or services) is received.

2.3.5.2 Disclosure

Since a measurement of a share-based payment award is not subject to ASC 820, the disclosure requirements of ASC 820 do not apply to share-based payments, regardless of whether such payments are granted to employees or nonemployees. Rather, fair-value-based measurements of share-based payments are subject to the disclosure requirements of ASC 718 (and ASC 505-50).
2.3.6 Assets Acquired and Liabilities Assumed in a Business Combination

2.3.6.1 Measurement

ASC 805-20-30-1 states that the acquirer in a business combination must measure the “identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree at their acquisition-date fair values.” However, ASC 820-10-15-3(e) notes that ASC 805-20-30-10 through 30-26 cite the following exceptions to this measurement principle:

- **Income taxes** — ASC 805-740-30-1 states that “[a]n acquirer shall measure a deferred tax asset or deferred tax liability arising from the assets acquired and liabilities assumed in a business combination in accordance with [ASC] 740-10.”

- **Employee benefits** — Under ASC 805-20-30-14 and 30-15, “[t]he acquirer shall measure a liability (or asset, if any) related to the acquiree’s employee benefit arrangements in accordance with other GAAP.” For example, an acquirer recognizes “an asset or a liability [equal to] the funded status of a single-employer defined benefit pension or postretirement plan” in accordance with ASC 805-20-25-23, ASC 805-20-25-25, and ASC 805-20-30-15. ASC 805-20-30-17 provides measurement-related guidance that applies to other employee benefit arrangements.

- **Indemnification assets** — The acquirer measures an indemnification asset on the same basis as the indemnified item. For example, if the seller in a business combination contractually indemnifies the acquirer for the outcome of an uncertain tax position, the indemnification asset would be measured on the same basis as the uncertain tax position (provided that there are no contractual limitations or collectibility is not in doubt). Also see the “Income taxes” bullet above. If the indemnified item is not measured at fair value, the indemnification asset would also not be measured at fair value.

- **Reacquired rights** — ASC 805-20-30-20 indicates that the acquirer measures the value of a reacquired right “on the basis of the remaining contractual term of the related contract regardless of whether market participants would consider potential contractual renewals in determining its fair value.”

- **Share-based payment awards** — Under ASC 805-20-30-21, the acquirer measures “a liability or an equity instrument related to the replacement of an acquiree’s share-based payment awards with share-based payment awards of the acquirer in accordance with the method in [ASC] 718.”

- **Assets held for sale** — Under ASC 805-20-30-22, the acquirer measures “an acquired long-lived asset (or disposal group) that is classified as held for sale at the acquisition date in accordance with [ASC] 360-10, at fair value less cost to sell.” The fair value measurement would be performed on the basis of the measurement guidance in ASC 820.

- **Certain assets and liabilities arising from contingencies** — ASC 805-20-30-23 indicates that if the fair value of an asset or liability assumed in a business combination that arises from a contingency cannot be determined during the measurement period, the asset or liability should be measured in accordance with ASC 450.

Upon an entity’s adoption of ASU 2016-02 and ASU 2016-13, the following two additional exceptions to the measurement principle in ASC 805-20-30-1 are also applicable:

- **Lease assets and lease liabilities** — ASC 805-20-30-24 and 30-25 contain specific guidance on measuring lease assets and lease liabilities when the acquiree is a lessee or lessor. This guidance applies upon the adoption of ASU 2016-02.
• **Purchased financial assets with credit deterioration** — Under ASC 805-20-30-26, which applies upon the adoption of ASU 2016-13, the acquirer recognizes “purchased financial assets with credit deterioration (including beneficial interests meeting the conditions in paragraph 325-40-30-1A) in accordance with Section 326-20-30 for financial instruments measured at amortized cost or Section 326-30-30 for available-for-sale debt securities.”

See Section 10.10.13 and Deloitte’s *A Roadmap to Accounting for Business Combinations* for further discussion of the initial recognition of assets acquired and liabilities assumed in a business combination.

### 2.3.6.2 Disclosure

Except for assets held for sale, assets acquired and liabilities assumed that are within the scope of the above exceptions would not be measured at fair value; the fair value disclosure requirements in ASC 820 thus would not apply to such assets and liabilities. While assets held for sale are measured on a fair value basis under ASC 820 (i.e., fair value less costs to sell), ASC 820’s disclosure requirements do not apply to fair value measurements at initial recognition. Rather, ASC 805 addresses the disclosures required for the assets acquired and liabilities assumed listed in Section 2.3.6.1 (see Section A.18).

### 2.3.7 Impairment Testing of Long-Lived Assets

#### 2.3.7.1 Measurement

##### 2.3.7.1.1 Long-Lived Assets Classified as Held and Used

When evaluating a long-lived asset (asset group) classified as held and used for impairment under ASC 360-10-35-16 through 35-36, an entity first performs a recoverability test by using undiscounted cash flows. If the long-lived asset (asset group) is not recoverable, the entity records an impairment loss, which is measured as the difference between the carrying amount and fair value of the long-lived asset (asset group). The fair value measurement guidance in ASC 820 applies to the measurement of the impairment loss. However, an impairment loss is not recognized if the carrying amount of the long-lived asset (asset group) is recoverable on the basis of the undiscounted cash flows expected to result from the asset’s use. The recoverability test is based on management’s intended use of the assets. If a long-lived asset (asset group) fails the recoverability test, the impairment loss is measured on the basis of market-participant assumptions in accordance with ASC 820.

When determining the fair value of a long-lived asset (asset group), entities must consider the highest and best use of the nonfinancial asset(s) from a market-participant perspective. ASC 820-10-35-10C states that the “[h]ighest and best use is determined from the perspective of market participants, even if the reporting entity intends a different use,” but clarifies that “a reporting entity's current use of a nonfinancial asset is presumed to be its highest and best use unless market or other factors suggest that a different use by market participants would maximize the value of the asset.” ASC 820 does not require entities to use a specific valuation technique when measuring the fair value of an asset or liability. However, ASC 360-10-35-36 indicates that for long-lived assets (asset groups) with uncertain cash flows, an expected-present-value technique is often the appropriate technique for measuring the fair value of long-lived assets. Simply discounting the cash flow projections used in the recoverability analysis may not be appropriate under ASC 820 because management may use assumptions in the recoverability analysis that are not market-participant assumptions. This is particularly the case when a market participant’s highest and best use is different from management’s intended use. To reflect market-participant assumptions, entities may need to adjust internally developed assumptions regarding their intended use of the asset when such assumptions are included in the projection of undiscounted cash flows and differ from market-participant assumptions.
2.3.7.1.2 Long-Lived Assets Classified as Held for Sale

A long-lived asset (asset group) classified as held for sale is measured at the lower of cost or fair value less costs to sell in accordance with ASC 360-10-35-37 through 35-45. The fair value measurement is subject to the measurement guidance in ASC 820.

2.3.7.1.3 Long-Lived Assets to Be Exchanged or to Be Distributed to Owners in a Spin-Off

ASC 360-10-40-4 addresses the accounting for long-lived assets (disposal groups) to be exchanged or distributed to owners in a spin-off. ASC 360-10-40-4 states, in part, that “[i]n addition to any impairment losses required to be recognized while the asset is classified as held and used, an impairment loss, if any, shall be recognized when the asset is disposed of if the carrying amount of the asset (disposal group) exceeds its fair value.” ASC 820 applies to the determination of fair value for this purpose.

2.3.7.2 Disclosure

The recognition of an impairment loss on a long-lived asset (asset group or disposal group) represents a nonrecurring fair value measurement that is subject to ASC 820’s disclosure requirements pertaining to nonrecurring fair value measurements. In addition, the disclosures required by ASC 360-10-50 include certain disclosures regarding fair value measurements. The disclosures in ASC 825-10-50-10 through 50-15 do not apply to long-lived assets. See Section A.9 for more information about the fair value disclosure requirements of ASC 360.

2.3.8 Leases

2.3.8.1 Measurement

2.3.8.1.1 Before Adoption of ASC 842

ASC 820-10-15-2(c) exempts from ASC 820’s measurement guidance the “accounting principles that address fair value measurements for purposes of lease classification or measurement in accordance with Topic 840.” Thus, ASC 820’s measurement guidance does not apply to estimating the residual value of a leased asset or determining whether a lease is classified as an operating or capital lease by the lessee (or an operating, sales-type, or direct financing lease by the lessor). Nevertheless, ASC 820’s measurement guidance does apply to any fair value measurement that is not related to lease classification or measurement. For example, ASC 820’s measurement guidance applies to the following:

- **Lessee’s accounting for a capital lease** — The lessee recognizes the leased asset when capital lease accounting applies. The leased asset is subject to the impairment guidance in ASC 360. Thus, if step 2 of the impairment test in ASC 360 requires the recognition of an impairment loss, the fair value of the capital lease asset should be estimated in accordance with the fair value measurement guidance in ASC 820. See Section 2.3.7.1 for more information.

- **Lessor’s accounting for an operating lease** — The lessor continues to recognize the leased asset when operating lease accounting applies. The leased asset is subject to the impairment guidance in ASC 360. Thus, if step 2 of the impairment test under ASC 360 requires the recognition of an impairment loss, the fair value of the long-lived asset underlying an operating lease should be estimated in accordance with the fair value measurement guidance in ASC 820. See Section 2.3.7.1 for more information.

Although ASC 820’s measurement guidance does not apply to lease classification and measurement under ASC 840, the principles in ASC 820 may be relevant to the determination of an asset’s fair value for lease classification and measurement purposes. Although it will often be straightforward to estimate the fair value of a leased asset (e.g., the leased asset or a similar asset could have been purchased for cash or a used-asset market exists), if the fair value is not available or is otherwise readily determinable, it may be appropriate to perform a fair value measurement on the basis of the depreciated replacement cost of a comparable asset.
• **Lessor’s accounting for termination of a capital lease** — In accordance with ASC 840-30-40-7, upon termination of a capital lease, the lessor may recognize the leased asset at its fair value. Such measurement should be estimated in accordance with the fair value measurement guidance in ASC 820.

• **Lessor’s accounting for an impairment of the residual value of a capital lease** — ASC 840-30-35-53 specifies that “[i]f a lessor sells substantially all of the minimum rental payments associated with a sales-type, direct financing, or leveraged lease and retains an interest in the residual value of the leased asset,” it should recognize an other-than-temporary impairment loss on the residual value interest on the basis of the fair value of the asset. Such measurement should be estimated in accordance with the fair value measurement guidance in ASC 820.

• **Acquirer’s accounting in a business combination** — There is no exception related to applying the measurement guidance in ASC 820 to lease assets and liabilities recognized in a business combination in accordance with ASC 805-20-30-1.

• **Lease-related liabilities in restructuring and exit activities** — ASC 420 requires an entity to recognize lease-related liabilities — other than those related to capital leases — that are part of an exit or disposal activity at fair value under ASC 820.

When the lessee or lessor does not recognize the asset underlying a lease, ASC 840 applies to the ongoing accounting for the lease, including any evaluation of impairment. In these situations, the measurement guidance in ASC 820 is not applicable. ASC 840-10-55-42 through 55-44 contain guidance on determining the fair value of leased property.

### 2.3.8.1.2 After Adoption of ASC 842

ASU 2016-02 deleted the exception in ASC 820-10-15-2(c). Therefore, with one exception, ASC 820’s measurement guidance applies to any fair value measurement under ASC 842, including a fair value measurement used to determine lease classification. ASC 842 contains guidance on fair value estimates required under ASC 842 (see also Section 10.10.15 and Deloitte’s *A Roadmap to Applying the New Leasing Standard*). It should also be noted, however, that ASC 805-20 contains specific guidance on the acquirer’s measurement of lease assets and lease liabilities in a business combination (see Section 2.3.6.1).

### 2.3.8.2 Disclosure

ASC 820’s disclosure requirements apply only to a nonrecurring fair value measurement determined in accordance with ASC 820 in connection with a lease arrangement. ASC 825-10-50-8(d) exempts lease contracts (other than a contingent obligation associated with a canceled lease and a guarantee of a third-party lease obligation, which are not lease contracts) from the fair value disclosure requirements in ASC 825-10-50-10 through 50-15. ASC 840 (for entities that have not adopted ASC 842) and ASC 842 prescribe other lease-related disclosure requirements.

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48 ASU 2019-01 amended ASC 842-30-55-17A to require lessors that are not manufacturers or dealers to use the cost of the underlying asset as the asset’s fair value at lease commencement. This cost would reflect any applicable volume or trade discounts as well as costs related to acquiring the asset, including sales taxes and delivery charges. “However, if there has been a significant lapse of time between the acquisition of the underlying asset and lease commencement, the definition of fair value [in ASC 820] shall be applied.” As a result of the amendments made by ASU 2019-01, the guidance on this topic in ASC 842 is similar to that in ASC 840. Moreover, ASC 842-10-55-3 and ASC 842-10-55-13 address considerations related to how a lease should be classified when it is not practical to determine the fair value of the underlying asset.
2.3.9 AROs

2.3.9.1 Measurement

Generally, ASC 820 applies to the initial measurement of an ARO. ASC 410-20-25-4 states that an entity should recognize the liability at its fair value “in the period in which it is incurred if a reasonable estimate of fair value can be made.” In addition, ASC 410-20-30-1 states, in part:

An expected present value technique will usually be the only appropriate technique with which to estimate the fair value of a liability for an asset retirement obligation. An entity, when using that technique, shall discount the expected cash flows using a credit-adjusted risk-free rate. Thus, the effect of an entity's credit standing is reflected in the discount rate rather than in the expected cash flows.

Further, ASC 410-20-25-4 states, in part, that “[i]f a reasonable estimate of fair value cannot be made in the period the [ARO] is incurred, the liability shall be recognized when a reasonable estimate of fair value can be made.” This practical expedient, which provides for a delay in the recognition of the ARO until its fair value is reasonably estimable, is also addressed in ASC 820-10-15-3(c).

The subsequent measurement of an ARO liability is subject to the guidance in ASC 410-20. ASC 410-20-35-3 through 35-8 provide guidance on recognizing the period-to-period changes in the liability as a result of (1) the passage of time and (2) revisions to the timing or amount of the estimated original undiscounted cash flows. This guidance can be summarized as follows.

- **Passage of time** — To measure changes in the liability related to the passage of time, an entity should apply an “interest method of allocation to the . . . liability at the beginning of the period” by using the “credit-adjusted risk-free rate that existed when the liability . . . was initially measured.”

- **Revisions to timing or amount of estimated undiscounted cash flows** — Upward revisions that create an incremental change in the undiscounted estimated cash flows should be discounted by using the current credit-adjusted risk-free rate, which adds an additional “layer” to the ARO liability. Downward revisions in estimated undiscounted cash flows are “discounted using the credit-adjusted risk-free rate that existed when the original liability was recognized.”

The changes resulting from the passage of time and revisions to estimated undiscounted cash flows are then incorporated into a remeasurement of the ARO. Although the fair value measurement concepts in ASC 820 apply to upward revisions to the ARO, the incremental layers are not separate liabilities. Therefore, subsequent measurements of the entire ARO are not fair value measurements.

See Section 10.10.7 for more information about the fair value measurement of AROs.

2.3.9.2 Disclosure

Because ASC 820’s disclosure requirements do not apply to fair value measurements at initial recognition and the subsequent measurement of an ARO is not a fair value measurement of the entire obligation, ASC 820’s disclosure requirements do not apply to AROs. However, ASC 410-20-50-2 states that “[i]f the fair value of an asset retirement obligation cannot be reasonably estimated, that fact and the reasons therefor shall be disclosed.” ASC 410-20-55-57 through 55-62 give examples of situations in which sufficient information is not available at the time the liability is incurred, as discussed in ASC 410-20-25-4. ASC 410-20-50 does not contain any disclosure requirements specific to fair value measurements of AROs (see Section A.10). The disclosures required by ASC 825-10-50-10 through 50-15 apply only to financial liabilities.
2.3.10 Life Insurance Contracts

2.3.10.1 Measurement

The measurement of a company-owned life insurance contract at CSV under ASC 325-30-35-2 does not represent a fair value measurement under ASC 820. Rather, CSV is a settlement value, not an amount that a market participant would pay to purchase the insurance contract from the policyholder. Company-owned life insurance contracts that are measured at fair value would, however, be subject to the measurement guidance in ASC 820.

ASC 325-30 discusses the accounting when a third-party investor purchases the future payment streams of life insurance policies from the policies' owners (referred to as life settlement contracts). Investors account for life settlement contracts by using either the investment method or fair value method. When using the investment method, an investor may write an investment down to fair value if it is impaired (see ASC 325-30-35-11). When an investment is impaired under the investment method or when the fair value method is used, the measurement guidance in ASC 820 applies.

Note that the above guidance related to CSV measurements under ASC 325-30 does not apply to sponsors of pension and other postretirement benefit plans. Under ASC 715-30-35-60 and ASC 715-60-35-120, CSV is presumed to be fair value if the life insurance contract is a pension plan asset or other postretirement plan asset, respectively.

In the financial statements of a pension or other postretirement benefit plan (under ASC 960, ASC 962, and ASC 965), company-owned life insurance contracts are “[measured] in the same manner as specified in the annual report filed by the plan with certain governmental agencies pursuant to the Employee Retirement Income Security Act; that is, either at fair value or at amounts determined by the insurance entity (contract value).” See ASC 960-325-35-3, ASC 962-325-35-6, and ASC 965-325-35-3 for more information.

2.3.10.2 Disclosure

Company-owned life insurance contracts recognized at CSV are not subject to ASC 820's disclosure requirements since such contracts are not carried at fair value. Company-owned life insurance contracts that are measured at fair value are subject to the disclosure requirements in ASC 820.

Life settlement contracts that are recognized at fair value are subject to ASC 820's disclosure requirements related to recurring fair value measurements. Life settlement contracts that are not recognized at fair value would be subject to ASC 820's disclosure requirements related to nonrecurring fair value measurements only in periods in which such contracts have been impaired and written down to their fair value.

Although CSV is considered fair value for pension reporting purposes, the disclosure requirements of ASC 820 do not apply to pension and other postretirement benefit plan assets within the plan sponsor's financial statements. 49

ASC 825-10-50-8(c) exempts insurance contracts from the disclosure requirements in ASC 825-10-50-10 through 50-15.

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49 Although a plan sponsor's disclosures about the fair value of pension and other postretirement benefit plan assets are not within the scope of ASC 820, ASC 715-20-50 contains similar applicable disclosure requirements.
2.3.11 Hedged Item in a Fair Value Hedge

2.3.11.1 Measurement

ASC 815-20-25-11 states that “[a]n entity may designate a derivative instrument as hedging the exposure to changes in the fair value of an asset or a liability or an identified portion thereof (hedged item) that is attributable to a particular risk” (emphasis added). The carrying value of the hedged item in a fair value hedge will generally not equal its fair value for two reasons. First, in a fair value hedge, an entity attempts to hedge the change in fair value of an asset or liability. Second, in a fair value hedge, an entity typically only hedges the change in fair value due to a particular risk (or risks), thereby excluding factors that would be included in a fair value measurement of the entire hedged item. Accordingly, the hedged item will equal fair value only if, (1) at inception of the hedging relationship, the hedged item is recorded at its fair value and (2) the entity hedges the entire change in fair value of the hedged item. These conditions are typically not met. In fact, in many cases in which the hedged item is a financial asset or liability, the entity would apply the FVO in lieu of hedge accounting.

Note that the measurement guidance in ASC 820 would always apply to the measurement of the change in fair value of the hedged item, even if the hedged item is not carried at fair value.

2.3.11.2 Disclosure

The remeasurement of the hedged item in a fair value hedge is subject to ASC 820’s disclosure requirements related to recurring fair value measurements only if the designated hedge results in recognition of the hedged item at fair value. Otherwise, only the disclosure requirements in ASC 815 and ASC 825 are applicable.

2.3.12 Nonmonetary Transactions

2.3.12.1 Measurement

ASC 845-10-30-1 states, in part, that “[i]n general, the accounting for nonmonetary transactions should be based on the fair values of the assets (or services) involved, which is the same basis as that used in monetary transactions.” When fair value is the basis of recognition for a nonmonetary transaction, the fair value measurement guidance in ASC 820 applies (i.e., the initial fair value measurement of the nonmonetary asset received should be determined in accordance with ASC 820). However, ASC 845-10-30-3 requires measurement of a nonmonetary exchange “based on the recorded amount . . . of the nonmonetary asset(s) relinquished, and not on the fair values of the exchanged assets,” if (1) the fair value is not “determinable within reasonable limits,” (2) the “transaction is an exchange of a product or property held for sale in the ordinary course of business for a product or property to be sold in the same line of business to facilitate sales to customers other than the parties to the exchange,” or (3) the “transaction lacks commercial substance.” These exceptions related to fair value measurements are acknowledged in ASC 820-10-15-3(c)(1). In the absence of an exception, the ASC 820 measurement guidance applies to fair value measurements recognized for nonmonetary transactions. See Section 10.10.16 for further discussion of the fair value measurement of nonmonetary transactions.

ASC 845-10-30-15 and 30-16 address the types of purchases and sales of inventory with the same counterparty that are measured at fair value.
2.3.12.2 Disclosure

ASC 820’s disclosure requirements do not apply to a nonmonetary transaction, even if it is recognized on the basis of a fair value measurement that is calculated in accordance with ASC 820, because ASC 820’s disclosure requirements do not apply to the initial recognition of an item at fair value. ASC 845-10-50-3 contains one fair-value-related disclosure requirement applicable to nonmonetary transactions (see Section A.21).

2.3.13 Exit or Disposal Cost Obligations

2.3.13.1 Measurement

ASC 420 requires an entity to initially measure a liability for a cost associated with an exit or disposal activity at fair value in the period in which the liability is incurred, except for certain one-time termination benefits that are incurred over time, which are initially recognized as of the communication date on the basis of the fair value of the liability as of the termination date. However, ASC 420-10-25-1 states the following about measuring restructuring obligations at fair value: “In the unusual circumstance in which fair value cannot be reasonably estimated, the liability shall be recognized initially in the period in which fair value can be reasonably estimated.” See Section 10.10.8 for further discussion of the fair value measurement of exit or disposal cost obligations.

2.3.13.2 Disclosure

ASC 820’s disclosure requirements do not apply to the initial recognition of an item at fair value. However, under ASC 420-10-50-1(e), “[i]f a liability for a cost associated with [an exit or disposal] activity is not recognized because fair value cannot be reasonably estimated,” an entity is required to disclose “that fact and the reasons why.” ASC 420-10-50 does not contain any disclosure requirements that apply to fair value measurements of exit or disposal obligations.

2.3.14 Noncash Consideration in a Revenue Contract

2.3.14.1 Measurement

ASC 820-10-15-2(d) contains an exception related to applying the fair value measurement guidance in ASC 820 to “the recognition and measurement of revenue from contracts with customers in accordance with Topic 606.” ASC 606 notes that fair value is the relevant measurement attribute in the following circumstances:

- The determination of the transaction price for contracts in which a customer promises a form of noncash consideration (ASC 606-10-32-21 and 32-22 and ASC 606-10-55-250).
- Changes in the fair value of noncash consideration after contract inception (ASC 606-10-32-23).
- Consideration that is payable to a customer and that is a payment for a distinct good or service received from the customer, which may reduce the transaction price (ASC 606-10-32-26).

ASC 606-10-32-21 states, in part, that “the transaction price for contracts in which a customer promises consideration in a form other than cash . . . [is] the estimated fair value of the noncash consideration at contract inception (that is, the date at which the criteria in paragraph 606-10-25-1 are met).” However, as noted in ASC 820-10-15-3(f)(1), ASC 606-10-32-22 contains an exception to initial measurement at fair value for entities that cannot reasonably estimate the fair value of the noncash consideration. ASC 606-10-32-22 indicates that entities that apply this practical expedient must “measure the consideration indirectly by reference to the standalone selling price of the goods or services promised to the customer (or class of customer) in exchange for the consideration.”
ASC 606 does not define fair value. While the ASC 820 fair value measurement guidance does not explicitly apply to the measurement of noncash consideration in a revenue contract, it may be relevant for entities to consider the measurement principles in ASC 820 in such circumstances. In addition, if another Codification topic requires an entity to measure a change in the fair value of noncash consideration, and such a change has no impact on the transaction price under ASC 606, the ASC 820 fair value measurement guidance must be applied to the recognition of such fair value measurements in the absence of a specific exception in the other Codification topic or ASC 820.

2.3.14.2 Disclosure

ASC 820's disclosure requirements do not apply to any fair value measurements under ASC 606 because (1) the initial recognition of an item at fair value is not subject to ASC 820's disclosure requirements and (2) any fair value measurement required under ASC 606 is not within the scope of ASC 820. However, ASC 606-10-50-20 specifies that entities are required to disclose the methods, inputs, and assumptions related to the transaction price in a revenue contract with a customer. In addition, when another Codification topic requires the fair value measurement of noncash consideration and such measurement is performed in accordance with ASC 820, the measurement is subject to ASC 820's disclosure requirements in the absence of a specific exception in the other Codification topic or ASC 820.

2.3.15 Defined Benefit Pension and Other Postretirement Plans in the Sponsor's Financial Statements

2.3.15.1 Measurement

2.3.15.1.1 Plan Assets

Under ASC 715-30 and ASC 715-60, sponsors of defined benefit pension and other postretirement plans recognize, in the statement of financial position, the funded status of the plan by offsetting the fair value of plan assets and the benefit obligation. Because plan assets are measured at fair value as of the measurement date, the measurement guidance in ASC 820 applies. Sponsors with postemployment benefits accounted for under ASC 712 that apply the measurement provisions of ASC 715-30 or ASC 715-60 should also apply the measurement guidance in ASC 820.

ASC 715-30 and ASC 715-60 contain an exemption related to the requirement to subsequently measure participation rights at fair value. ASC 715-30-35-58 and ASC 715-60-35-116 state, in part:

> [T]he participation right shall be measured at its fair value if the contract is such that fair value is reasonably estimable. Otherwise, the participation right shall be measured at its amortized cost (not in excess of its net realizable value), and the cost shall be amortized systematically over the expected dividend period under the contract.

2.3.15.1.2 Plan Obligations

The pension or postretirement benefit obligation under ASC 715 is not measured at fair value; rather, it is an actuarial present value calculation of estimated future benefit costs that is based on employee services rendered to date. Therefore, ASC 820 does not apply to such measurement.

51 ASC 715-30-35-50 indicates that the fair value of an investment should reflect "brokerage commissions and other costs normally incurred in a sale if those costs are significant (similar to fair value less cost to sell)." See Section 10.10.11 for further discussion of the fair value measurement of assets in a defined benefit pension or other postretirement plan.
2.3.15.2 Disclosure

Although ASC 820 applies to the measurement of plan assets, the disclosure requirements of ASC 820 do not apply to plan assets accounted for under ASC 715 in the sponsor's financial statements. ASC 820-10-50-10 states that “[p]lan assets of a defined benefit pension or other postretirement plan that are accounted for in accordance with Topic 715 are not subject to the disclosure requirements [of ASC 820]. Instead, the disclosures required in [ASC] 715-20-50-1(d)(iv) and 715-20-50(c)(iv) shall apply for fair value measurements of plan assets of a defined benefit pension or other postretirement plan.” Sponsors with postemployment benefits accounted for under ASC 712 that apply the measurement provisions of ASC 715-30 or ASC 715-60 should also apply the disclosure requirements of ASC 715-20-50. The disclosure requirements in ASC 825-10-50-10 through 50-15 apply to plan assets (except for insurance contracts and FBRICs), which are generally measured at fair value. However, ASC 825-10-50-8(a) exempts benefit obligations from these disclosure requirements. Rather, benefit obligations are subject to the disclosure requirements of ASC 715. See Section A.16 for further discussion of the fair value disclosure requirements in ASC 715-20-50.

2.3.16 Financial Statements of Defined Benefit Plans, Defined Contribution Plans, and Health and Welfare Plans

2.3.16.1 Measurement

2.3.16.1.1 Plan Assets

ASC 820 applies to the fair value measurement of pension plan investments in accordance with ASC 960 as well as to that of plan investments held within a defined contribution pension plan, which must be measured at fair value as of the reporting date in accordance with ASC 962. However, participant loans are not considered plan investments and should not be measured at fair value. The measurement guidance in ASC 820 further applies to investments held within health and welfare benefit plans, which must be measured at fair value in accordance with ASC 965. See Sections 10.10.19.9 and 10.10.19.10 for further discussion of fair value measurements under ASC 962 and ASC 965.

2.3.16.1.2 Plan Obligations

ASC 820 does not apply to accumulated plan benefit obligations, which are not measured at fair value; rather, such obligations are measured on the basis of an actuarial present value calculation of future benefits that are attributable to plan participants for services rendered to date in accordance with the provisions of the plan.

2.3.16.2 Disclosure

ASC 820's disclosure requirements apply to pension plan investments that an entity must measure at fair value in accordance with ASC 960, plan investments held within a defined contribution pension plan that must be measured at fair value in accordance with ASC 962, and investments held within health and welfare benefit plans that must be measured at fair value in accordance with ASC 965. Because such plan assets must be measured at fair value as of each reporting date, the financial statements of such plans must include the recurring fair value disclosures required under ASC 820. ASC 960, ASC 962, and ASC 965 also contain specific disclosure requirements, including those related to fair value and certain references to the disclosures required by ASC 820. The disclosures in ASC 825-10-50-10 through 50-15 also apply to plan investments, except for insurance contracts and FBRICs. See Sections A.32 through

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52 ASC 960-325-35-2 indicates that “[i]f significant, the fair value of an investment shall be reduced by brokerage commissions and other costs normally incurred in a sale (similar to fair value less cost to sell).”

53 In accordance with ASC 962-310-35-2, “participant loans [are] measured at their unpaid principal balance plus any accrued but unpaid interest.”
A.34 for further discussion of the incremental fair-value-related disclosures required by ASC 960, ASC 962, and ASC 965.

The fair value disclosures required by ASC 820 do not apply to plan benefit obligations under ASC 960, ASC 962, and ASC 965. Furthermore, ASC 825-10-50-8(a) exempts such plan obligations from the disclosure requirements of ASC 825-10-50-10 through 50-15. In such cases, entities should look to the respective disclosure requirements of ASC 960, ASC 962, and ASC 965.

2.3.17 Deferred Compensation Obligations in Rabbi Trusts

2.3.17.1 Measurement

Many employers enter into deferred compensation arrangements that allow employees to defer some or all of their earned compensation (i.e., salary or bonus). Deferred compensation contracts that are not considered equivalent to a postretirement income or health or welfare benefit plan are generally accounted for under ASC 710 or ASC 718.

Sometimes the employer uses a “rabbi trust” to hold assets from which distributions will be made as part of a nonqualified deferred compensation plan. ASC 710 provides guidance on deferred compensation arrangements in which assets equal to compensation amounts earned by employees are placed in a rabbi trust. ASC 710-10-25-15 describes four types of such arrangements and states:

The following are the four types of deferred compensation arrangements involving rabbi trusts covered by this Subsection:

a. Plan A — The plan does not permit diversification and must be settled by the delivery of a fixed number of shares of employer stock.
b. Plan B — The plan does not permit diversification and may be settled by the delivery of cash or shares of employer stock.
c. Plan C — The plan permits diversification; however, the employee has not diversified (the plan may be settled in cash, shares of employer stock, or diversified assets).
d. Plan D — The plan permits diversification and the employee has diversified (the plan may be settled in cash, shares of employer stock, or diversified assets).

ASC 710-10-35-2 states that changes in the fair value of the deferred compensation obligation of Plan A “shall not be recognized,” and ASC 825-10-15-5(c) and 15-5(f) preclude an entity from applying the FVO to this obligation. ASC 710-10-35-3 and 35-4 state that the deferred compensation obligations of Plans B, C, and D “shall be adjusted with a corresponding charge (or credit) to compensation cost, to reflect the changes in the fair value of the amount owed to the employee.” ASC 710-10-45-2 further states that “[f]or Plan D only, changes in the fair value of the deferred compensation obligation shall not be recorded in other comprehensive income, even if changes in the fair value of the assets held by the rabbi trust are recorded, pursuant to Subtopic 320-10, in other comprehensive income.”

While the fair value adjustments to the deferred compensation obligations of Plans B and C must be measured in accordance with ASC 820, the deferred compensation obligation of Plan D does not need to represent a fair value measurement in accordance with ASC 820. Discussions with the FASB staff have indicated that obligations for Plan D deferred compensation arrangements, as described in ASC 710, are not fair value measurements subject to the requirements of ASC 820. The intent of the guidance was to have the obligation match the fair value of the amounts earned and assets held in the rabbi trust. This intent is consistent with the original transition guidance in EITF Issue 97-14, which states, in part, “For

54 For Plans A, B, and C, the employer stock held by the rabbi trust is classified as equity in a manner similar to the accounting for treasury stock (see ASC 710-10-25-16 and 25-17). For Plan D, assets held by the rabbi trust are accounted for in accordance with other Codification topics (e.g., ASC 320 or ASC 321) (see ASC 710-10-25-18).
Plan D, the diversified assets held by the rabbi trust should be recorded at fair value at September 30, 1998 with a corresponding amount recorded as a deferred compensation liability (emphasis added). In other words, the liability was not reported at fair value as of the transition; rather, it was set to equal the fair value of the assets held in the rabbi trust.55 Thus, the nonperformance risk associated with the obligation would not be reflected in its measurement.

Note that other deferred compensation arrangements allow participants to “invest” their earned compensation into “phantom” investments indexed to employer stock, nonemployer securities, or a combination of both; however, the employer does not purchase investments that are held separately in a trust. The amount due (i.e., the obligation) to employees in each reporting period represents deferred pay plus or minus the changes in fair value of the phantom investments. Entities with phantom deferred compensation arrangements whose employees have diversified their accounts into nonemployer securities may apply, by analogy, the Plan D accounting guidance in ASC 710 to measure the obligation.

2.3.17.2 Disclosure

For Plan A, the fair value measurement disclosures required by ASC 820 and ASC 825 do not apply, since both the employer stock held by the rabbi trust and any deferred compensation obligation are classified in equity in accordance with ASC 710-10-25-16. ASC 825-10-50-8(l) exempts equity instruments from the disclosure requirements of ASC 825-10-50-10 through 50-15.

For Plans B and C, the fair value measurement disclosures required by ASC 820 and ASC 825 do not apply to the employer stock held by the rabbi trust since those shares are classified in equity. ASC 825-10-50-8(l) exempts equity instruments from the disclosure requirements of ASC 825-10-50-10 through 50-15. The deferred compensation obligation, however, is subject to ASC 820’s disclosure requirements related to recurring fair value measurements. ASC 825-10-50-8(a) exempts the obligation from the disclosure requirements of ASC 825-10-50-10 through 50-15.

For Plan D, the fair value measurement disclosures required by ASC 820 and ASC 825 apply to the assets held by the rabbi trust in the absence of a specific exception. Because the obligations are not fair value measurements, the ASC 820 fair value disclosures are not required. ASC 825-10-50-8(a) also exempts the obligation from the disclosure requirements of ASC 825-10-50-10 through 50-15.

ASC 710 does not require entities to provide any specific disclosures about these arrangements.

2.3.18 Contributions

2.3.18.1 Measurement

ASC 720-25-30-2 states that an entity’s obligation for “[u]nconditional promises to give that are expected to be paid in less than one year may be measured at net settlement value because that amount, although not equivalent to the present value of estimated future cash flows, results in a reasonable estimate of fair value.” This provision effectively represents a practical expedient related to a fair value measurement.

ASC 958-605-25-4 states, with respect to an NFP entity’s revenue recognition, that “[a] major uncertainty about the existence of value may indicate that an item received or given should not be recognized.” The AICPA Industry Audit Guide Audits of Voluntary Health and Welfare Organizations indicates that “[b]ecause of the difficulty of placing a monetary value on donated services, and the absence of control over them, the value of these services often is not recorded as contributions and expense.” This provision represents

55 On the basis of inquiries with the FASB staff, we believe that ASC 815 did not change the Plan D accounting guidance in ASC 710; therefore, deferred compensation arrangements in which an entity applies the Plan D accounting guidance in ASC 710 are not within the scope of ASC 815.
an exception from the requirement for an NFP entity to measure contributions received at fair value in accordance with ASC 958-605-30-2. See Section 10.10.19.8 for further discussion of the fair value measurement requirements of ASC 958.

2.3.18.2 Disclosure

ASC 820’s fair value disclosure requirements do not apply to the measurements referred to in Section 2.3.18.1 because these requirements do not apply to initial measurements. ASC 720 does not have any specific disclosure requirements for unconditional promises to give. Further, ASC 958 also does not have any specific disclosure requirements related to situations in which a contribution received is not recognized as a result of a major uncertainty. However, entities may find that the disclosure in ASC 958-605-50-2 is relevant by analogy. ASC 958 does contain other fair-value-related disclosure requirements (see Section A.31).
3.1 Introduction
ASC 820 establishes a framework for measuring fair value and requires disclosures about fair value measurements. ASC 820-10-20 defines fair value as the “price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.” Thus, a fair value measurement is an “exit price.” As discussed below, an entity needs to perform various steps to (1) prepare a fair value measurement that complies with the measurement principles in ASC 820 and (2) meet the disclosure requirements in ASC 820.

3.2 Fair Value Application Framework

3.2.1 Step-by-Step Application Framework
An entity may apply the following step-by-step approach to measure and disclose fair value when other Codification topics require (or permit) the initial or subsequent measurement of an asset, liability, or equity instrument at fair value.

CERTAIN OF THE STEPS DESCRIBED ABOVE MAY BE INTERRELATED; THEREFORE, THESE STEPS DO NOT NECESSARILY HAVE TO BE PERFORMED IN THE ORDER SHOWN.
3.2.2 Step 1 — Identify the Unit of Account

**The Asset or Liability**

35-2D The asset or liability measured at fair value might be either of the following:

   a. A standalone asset or liability (for example, a financial instrument or a nonfinancial asset)
   b. A group of assets, a group of liabilities, or a group of assets and liabilities (for example, a reporting unit or a business).

35-2E Whether the asset or liability is a standalone asset or liability, a group of assets, a group of liabilities, or a group of assets and liabilities for recognition or disclosure purposes depends on its unit of account. The unit of account for the asset or liability shall be determined in accordance with the Topic that requires or permits the fair value measurement, except as provided in this Topic.

An asset, liability, or instrument classified in stockholders’ equity that is measured at fair value should be identified on the basis of its unit of account. Although ASC 820 defines fair value and establishes a framework for measuring it, the standard does not specify when items should be recognized at fair value in an entity's financial statements. With one exception, ASC 820 also does not specify the unit of account that applies to a particular fair value measurement. Therefore, entities must consult other Codification topics to determine (1) when an entity is required (or permitted) to initially or subsequently measure an asset, liability, or equity instrument at fair value and (2) the unit of account that applies to such a fair value measurement.

As discussed in Chapter 4, the unit of account represents the level of aggregation or disaggregation of individual assets, liabilities, or equity instruments for recognition in the financial statements and, with one exception, is determined on the basis of the guidance in other Codification topics. As discussed in Chapter 5, the unit of valuation is the grouping of assets, liabilities, or equity instruments for fair value measurement purposes. ASC 820 provides guidance on determining the unit of valuation (see Section 3.2.3 and Chapter 5 for more information). The unit of account may differ from the unit of valuation. In addition, entities may need to allocate fair value measurements even when the unit of account and unit of valuation are the same.

**Example 3-1**

**Impairment of Long-Lived Assets**

Under ASC 360, the unit of account for impairment testing is the asset group. However, the asset group is not the unit of account for recognition purposes. Rather, each of the individual long-lived assets represents a single unit of account. Therefore, in accordance with ASC 360-10-35-28, an entity must allocate the difference between the fair value of the asset group and the carrying amount of the asset group (i.e., the amount of impairment) to individual long-lived assets within the asset group. This allocation is required even if the unit of valuation for purposes of the fair value measurement is the asset group.

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1 ASC 820-10-35-44 specifies the unit of account (which is also the unit of valuation) that exists when an entity “holds a position in a single asset or liability (including a position comprising a large number of identical assets or liabilities, such as a holding of financial instruments) and the asset or liability is traded in an active market.” See Section 4.2 for more information.

2 See footnote 1.
Groups of Financial Assets and Financial Liabilities With Offsetting Risk Positions

An entity may have the option of grouping financial assets, financial liabilities, and nonfinancial items accounted for as derivatives under ASC 815, or a combination of those items, and measuring the portfolio’s fair value on the basis of its net risk position. In this case, the portfolio is the unit of valuation (see ASC 820-10-35-18D through 35-18L). However, each individual item in the portfolio represents a single unit of account. As a result, the portfolio-based fair value measurement must be allocated to the individual units of account within the portfolio.

See Chapter 4 for more information about the unit of account.

3.2.3 Step 2 — Identify the Unit of Valuation

3.2.3.1 Financial Assets, Nonfinancial Derivative Assets, Liabilities, and Equity Instruments

As discussed in Section 4.3.2, the unit of valuation for financial assets, nonfinancial derivative assets, liabilities, and equity instruments is the individual asset, liability, or equity instrument, which is generally also its unit of account under other GAAP. The concept of the “highest and best use” does not apply to fair value measurements of financial assets, nonfinancial derivative assets, liabilities, or instruments classified in stockholders’ equity.

Note that for liabilities and instruments classified in stockholders’ equity, an entity performing a fair value measurement assumes that the liabilities or equity instruments are transferred to a market participant on the measurement date. That is, ASC 820 requires entities measuring the fair value of a liability to assume that the liability remains outstanding and is transferred to a market-participant transferee that would be required to fulfill the obligation. Similarly, entities must assume that an instrument classified in stockholders’ equity would remain outstanding and that a market-participant transferee would take on the rights and responsibilities associated with the instrument. A liability being measured at fair value would not be assumed to be settled, and an instrument classified in shareholders’ equity would not be assumed to be canceled or otherwise extinguished. However, when a quoted price for the transfer of an identical or similar liability or an entity’s own equity instrument is not available and the identical item is held by another party as an asset, the entity must measure the fair value of the liability or its own equity instrument from the perspective of a market participant that holds the identical item as an asset. See Section 10.2.7 for more information.
3.2.3.1.1 Portfolio Valuation Exception for Certain Groups of Assets and Liabilities With Offsetting Risk Positions

**ASC 820-10**

<table>
<thead>
<tr>
<th>Application to Financial Assets and Financial Liabilities with Offsetting Positions in Market Risks or Counterparty Credit Risk</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>35-18D</strong> A reporting entity that holds a group of financial assets and financial liabilities is exposed to market risks (that is, interest rate risk, currency risk, or other price risk) and to the credit risk of each of the counterparties. If the reporting entity manages that group of financial assets and financial liabilities on the basis of its net exposure to either market risks or credit risk, the reporting entity is permitted to apply an exception to this Topic for measuring fair value. That exception permits a reporting entity to measure the fair value of a group of financial assets and financial liabilities on the basis of the price that would be received to sell a net long position (that is, an asset) for a particular risk exposure or paid to transfer a net short position (that is, a liability) for a particular risk exposure in an orderly transaction between market participants at the measurement date under current market conditions. Accordingly, a reporting entity shall measure the fair value of the group of financial assets and financial liabilities consistently with how market participants would price the net risk exposure at the measurement date.</td>
</tr>
</tbody>
</table>

**Pending Content (Transition Guidance: ASC 105-10-65-5)**

| **35-18D** A reporting entity that holds a group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items is exposed to market risks (that is, interest rate risk, currency risk, or other price risk) and to the credit risk of each of the counterparties. If the reporting entity manages that group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items on the basis of its net exposure to either market risks or credit risk, the reporting entity is permitted to apply an exception to this Topic for measuring fair value. That exception permits a reporting entity to measure the fair value of a group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items on the basis of the price that would be received to sell a net long position (that is, an asset) for a particular risk exposure or paid to transfer a net short position (that is, a liability) for a particular risk exposure in an orderly transaction between market participants at the measurement date under current market conditions. Accordingly, a reporting entity shall measure the fair value of the group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items consistently with how market participants would price the net risk exposure at the measurement date. |

An exception to ASC 820’s general principles related to the unit of valuation is available for groups of financial assets and financial liabilities if an entity (1) manages the group of assets and liabilities on the basis of net exposure to a market risk (or risks) or counterparty credit risk, (2) provides information on that basis to management, and (3) measures those assets and liabilities at fair value in the statement of financial position. To use the exception, an entity must make an accounting policy decision. Once the policy is established, the entity must consistently apply the policy from period to period for a particular portfolio. See Sections 4.3.2.1 and 5.3 for more information.

**Changing Lanes**

ASU 2018-09 amended ASC 820-10-35-18D to provide for a unit of valuation on the basis of a group that includes, in addition to financial assets and financial liabilities, nonfinancial items accounted for as derivatives in accordance with ASC 815, or combinations of these items. To use the exception, an entity must make an accounting policy decision. Once the policy is established, the entity must consistently apply the policy from period to period for a particular portfolio. See Sections 4.3.2.1 and 5.3 for more information.
3.2.3.1.2 Liabilities With Third-Party Credit Enhancements

The unit of account for a liability issued with an inseparable third-party credit enhancement is the liability, excluding the credit enhancement. See Section 4.3.2.2 for further discussion.

3.2.3.2 Nonfinancial Assets Other Than Nonfinancial Derivative Assets

The unit of valuation (also referred to as the “valuation premise”) for nonfinancial assets (other than nonfinancial derivative assets) is the asset’s highest and best use. ASC 820-10-20 defines the highest and best use as the “use of a nonfinancial asset by market participants that would maximize the value of the asset or the group of assets and liabilities (for example, a business) within which the asset would be used.” The highest and best use must be determined from the market participant’s perspective, regardless of the reporting entity’s current use. However, an entity is not required to perform an exhaustive search to identify the highest and best use and may presume that its current use is the highest and best use unless market or other factors suggest otherwise. The highest and best use of an asset might provide maximum value through its use either (1) in combination with other assets or other assets and liabilities or (2) on a stand-alone basis. See Section 5.2 for more information.

3.2.4 Step 3 — Identify the Principal or Most Advantageous Market

Underlying the fair value measurement objective in ASC 820 is the concept of an entity transacting in the principal market for the asset or liability (or equity instrument), or in the absence of a principal market, the most advantageous market. ASC 810-10-20 defines the principal market as the “market with the greatest volume and level of activity for the asset or liability” and the most advantageous market as the “market that maximizes the amount that would be received to sell the asset or minimizes the amount that would be paid to transfer the liability, after taking into account transaction costs and transportation costs.” The determination of the principal (or most advantageous) market for an asset, liability, or equity instrument can affect the fair value measurement since the exit price may differ from market to market. The concept of a most advantageous market is relevant only if there is no principal market for the asset, liability, or equity instrument subject to the fair value measurement.

An entity identifies the principal (or most advantageous) market for the asset or liability (or equity instrument) by first identifying all markets that it can access to sell the asset or transfer the liability. ASC 820-10-35-6A requires that an entity have access to the principal (or most advantageous) market. Then, the entity determines, from the perspective of market participants, which market has the greatest volume or level of activity (or in the absence of a principal market, which market maximizes the fair
value of the asset or minimizes the fair value of the liability). If there is a principal market, the fair value measurement should represent the price in that market, even if the price in a different market is potentially more advantageous. ASC 820-10-35-5A clarifies that an entity is not required to perform an exhaustive search to identify all markets. In fact, unless contradictory evidence exists, it is generally presumed that the market in which the reporting entity normally transacts is the principal (or most advantageous) market. See Chapter 6 for more information.

3.2.5 Step 4 — Develop Assumptions That Market Participants Would Use to Measure Fair Value

<table>
<thead>
<tr>
<th>ASC 820-10</th>
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<tbody>
<tr>
<td><strong>Market Participants</strong></td>
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<tr>
<td><strong>35-9</strong> A reporting entity shall measure the fair value of an asset or a liability using the assumptions that market participants would use in pricing the asset or liability, assuming that market participants act in their economic best interest. In developing those assumptions, a reporting entity need not identify specific market participants. Rather, the reporting entity shall identify characteristics that distinguish market participants generally, considering factors specific to all of the following:</td>
</tr>
<tr>
<td>a. The asset or liability</td>
</tr>
<tr>
<td>b. The principal (or most advantageous) market for the asset or liability</td>
</tr>
<tr>
<td>c. Market participants with whom the reporting entity would enter into a transaction in that market.</td>
</tr>
</tbody>
</table>

To meet the “exit price” measurement objective, an entity is required to develop assumptions that market participants would use to determine the price of an asset, liability, or equity instrument in an orderly transaction as of the measurement date. ASC 820-10-20 defines market participants as “buyers and sellers in the [entity’s] principal (or most advantageous) market for the asset or liability” that are (1) “independent of each other,” (2) knowledgeable, (3) “able to enter into a transaction for the asset or liability,” and (4) “willing to enter into a transaction for the asset or liability.” As noted in ASC 820-10-35-9, an entity “need not identify specific market participants” but should “identify characteristics that distinguish market participants generally.” The assumptions that market participants would use when measuring the fair value of the asset, liability, or equity instrument are relevant in the determination of the inputs to the fair value measurement. An entity may not substitute the assumptions of market participants with its own assumptions that differ from those of market participants. See Chapter 7 for more information.

3.2.6 Step 5 — Measure Fair Value on the Basis of Available Inputs and Appropriate Valuation Techniques

<table>
<thead>
<tr>
<th>ASC 820-10</th>
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| **30-2** When an asset is acquired or a liability is assumed in an exchange transaction for that asset or liability, the transaction price is the price paid to acquire the asset or received to assume the liability (an entry price). In contrast, the fair value of the asset or liability is the price that would be received to sell the asset or paid to transfer the liability (an exit price). Entities do not necessarily sell assets at the prices paid to acquire them. Similarly, entities do not necessarily transfer liabilities at the prices received to assume them.
In many cases, the transaction price will equal the fair value (for example, that might be the case when on the transaction date the transaction to buy an asset takes place in the market in which the asset would be sold).

When determining whether fair value at initial recognition equals the transaction price, a reporting entity shall take into account factors specific to the transaction and to the asset or liability. For example, the transaction price might not represent the fair value of an asset or a liability at initial recognition if any of the following conditions exist:

- a. The transaction is between related parties, although the price in a related party transaction may be used as an input into a fair value measurement if the reporting entity has evidence that the transaction was entered into at market terms.

- b. The transaction takes place under duress or the seller is forced to accept the price in the transaction. For example, that might be the case if the seller is experiencing financial difficulty.

- c. The unit of account represented by the transaction price is different from the unit of account for the asset or liability measured at fair value. For example, that might be the case if the asset or liability measured at fair value is only one of the elements in the transaction (for example, in a business combination), the transaction includes unstated rights and privileges that are measured separately, in accordance with another Topic, or the transaction price includes transaction costs.

- d. The market in which the transaction takes place is different from the principal market (or most advantageous market). For example, those markets might be different if the reporting entity is a dealer that enters into transactions with customers in the retail market, but the principal (or most advantageous) market for the exit transaction is with other dealers in the dealer market.

In all cases, a reporting entity shall maximize the use of relevant observable inputs and minimize the use of unobservable inputs to meet the objective of a fair value measurement, which is to estimate the price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions.

A reporting entity shall use valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

The objective of using a valuation technique is to estimate the price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions. Three widely used valuation approaches are the market approach, cost approach, and income approach. The main aspects of valuation techniques consistent with those approaches are summarized in paragraphs 820-10-55-3A through 55-3G. An entity shall use valuation techniques consistent with one or more of those approaches to measure fair value.

ASC 820 applies at both initial recognition and subsequent measurement if fair value is required or permitted by other Codification topics. On initial recognition, the transaction price, which is an entry price, will often equal fair value, which is an exit price. However, as discussed in ASC 820-10-30-3A, the transaction price may not equal fair value at initial recognition in certain situations. In such cases, an inception gain or loss may arise upon initial recognition of an asset or liability. See Chapter 9 for more information about the initial measurement of an item at fair value.
Since a fair value measurement is an exit price, a quoted market price for the identical asset, liability, or equity instrument (i.e., a Level 1 input) constitutes the most reliable evidence of fair value and, when available, must be used to measure fair value without being adjusted, except in limited circumstances. When a Level 1 input is not available to measure the fair value of an asset, liability, or equity instrument in its entirety, an entity will need to measure fair value by using one or more appropriate valuation techniques that incorporate available inputs. An entity must maximize relevant observable inputs (i.e., Level 1 and Level 2 inputs) and use unobservable inputs (i.e., Level 3 inputs) only when relevant observable inputs are not available. See Chapter 8 for more information about the fair value hierarchy.

An entity measures fair value on the basis of one or more of the three valuation approaches outlined in ASC 820-10-35-24A: (1) the market approach, (2) the income approach, or (3) the cost approach. Further, the entity selects one or more techniques “that are appropriate in the circumstances and for which sufficient data are available” to maximize the use of observable inputs while minimizing the use of unobservable inputs. If multiple techniques are used, the entity should evaluate the resultant range and should select a point within the range that is most representative of fair value.

The entity should evaluate the factors listed in ASC 820-10-35-54C to determine whether there has been a significant decrease in the volume and level of activity for the asset or liability in relation to normal market activity. This determination will affect the entity’s selection of techniques or inputs and the weight placed on quoted prices. If the volume and level of activity for the asset or liability have significantly decreased, the entity may need to significantly adjust the transaction or quoted price. Regardless, the entity’s objective is to select an estimate that is most representative of fair value.

See Chapter 10 for more information about the measurement of fair value on the basis of available inputs and appropriate valuation techniques.

3.2.7 Step 6 — Allocate Fair Value Measurement to Individual Units of Account (If Necessary)

As discussed in step 1, the unit of account may differ from the unit of valuation. In addition, an entity may need to perform allocations of fair value measurements even when the unit of account and unit of valuation are the same. In these circumstances, once the fair value is calculated at the level of the unit of valuation (see step 5), the entity must allocate the fair value measurement to the individual units of account that are subject to the fair value measurement. Since ASC 820 does not specify how to perform this allocation, the entity must consider the individual facts and circumstances, along with other relevant Codification topics, in such cases. See Section 4.3 for more information.

3.2.8 Step 7 — Classify the Fair Value Measurement Under the Fair Value Hierarchy and Prepare Disclosures

ASC 820 categorizes inputs used in fair value measurements into a three-level fair value hierarchy. An unadjusted quoted price in an active market is the most reliable measure of fair value and is categorized as Level 1. Fair value measurements that incorporate observable inputs (i.e., quoted market prices in active markets for similar assets or liabilities, quoted prices in inactive markets for identical or similar assets or liabilities, or other inputs that are observable or that can be corroborated through observable market data or in other ways for substantially the entire term of the assets or liabilities) represent Level 2 fair value measurements. Fair value measurements that incorporate unobservable inputs represent Level 3 fair value measurements. A fair value measurement that includes multiple inputs is categorized in its entirety on the basis of the lowest-level input that is significant to the entire measurement. In addition to requiring entities to classify fair value measurements within the fair value hierarchy, ASC 820 requires entities to provide various disclosures on the basis of such classification. See Chapters 8 and 11 for more information.
Chapter 4 — Unit of Account

4.1 Introduction

ASC 820-10

The Asset or Liability

35-2D The asset or liability measured at fair value might be either of the following:
   a. A standalone asset or liability (for example, a financial instrument or a nonfinancial asset)
   b. A group of assets, a group of liabilities, or a group of assets and liabilities (for example, a reporting unit or a business).

35-2E Whether the asset or liability is a standalone asset or liability, a group of assets, a group of liabilities, or a group of assets and liabilities for recognition or disclosure purposes depends on its unit of account. The unit of account for the asset or liability shall be determined in accordance with the Topic that requires or permits the fair value measurement, except as provided in this Topic.

The Fair Value Measurement Approach

55-1 The objective of a fair value measurement is to estimate the price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions. A fair value measurement requires a reporting entity to determine all of the following:
   a. The particular asset or liability that is the subject of the measurement (consistent with its unit of account)
   b. For a nonfinancial asset, the valuation premise that is appropriate for the measurement (consistent with its highest and best use)
   c. The principal (or most advantageous) market for the asset or liability
   d. The valuation technique(s) appropriate for the measurement, considering the availability of data with which to develop inputs that represent the assumptions that market participants would use when pricing the asset or liability and the level of the fair value hierarchy within which the inputs are categorized.

As discussed in Chapter 3, one of the requirements for a fair value measurement is that an entity must determine the particular asset, liability, or equity instrument that is subject to the measurement on the basis of its unit of account. ASC 820-10-20 defines the unit of account as “the level at which an asset or a liability is aggregated or disaggregated in a Topic for recognition purposes.” The unit of account is used to determine what is being measured by reference to the level at which the asset or liability is aggregated (or disaggregated) for accounting recognition or disclosure purposes. The unit of account could be a stand-alone asset, liability, or equity instrument; a group of assets; a group of liabilities; or a group of assets and liabilities.
Although ASC 820 defines fair value and establishes a framework for measuring it, the standard does not specify what items should be recognized at fair value in an entity's financial statements. The requirement (or ability) to measure an asset, liability, or equity instrument at fair value and the unit of account for such recognition is generally determined in accordance with the guidance in Codification topics other than ASC 820. With one exception, ASC 820 does not specify the unit of account to be used in a fair value measurement. See Table 2-1 for other Codification topics that specify the unit of account that applies to the recognition of an asset, liability, or equity instrument at fair value.

Examples 4-1 and 4-2 illustrate the determination of the unit of account.

### Example 4-1

**Unit of Account for Investments in Multiple Classes of an Investee Fund**

Entity A holds equity investments in multiple classes of an investee fund. The investee fund uses multiple share classes to help investors distinguish between various liquidity restrictions pertaining to their investments.

Entity A holds $3 million in Class A of the investee fund, which is redeemable at any point, and $500,000 in Class B (a restricted class such as an investment that was side-pocketed or that has other redemption lock-up provisions) of the investee fund, which is subject to a six-month lockout period. Assume that A would categorize the Class A investment within Level 2 of the fair value hierarchy and the Class B investment within Level 3 of the fair value hierarchy. Further assume that neither investment is measured by using the practical expedient for assets measured at NAV.

While Class A and Class B may be part of the same subscription agreement, the characteristics of the equity investments in the two classes differ (i.e., Class B is restricted and Class A is not). Therefore, in this example, the two classes are considered separate units of account under ASC 321. Accordingly, it would not be appropriate to combine Class A and Class B into a single unit of account and, for example, classify the combined unit as Level 2 or Level 3 in its entirety. Rather, A must perform a separate analysis of Class A and Class B for ASC 820 disclosure purposes (i.e., A must separately determine the level in the fair value hierarchy in which each investment is categorized). This same principle would also apply to investments in partnership entities that have different classes of partnership interests.

### Example 4-2

**Debt Instrument With a Third-Party Credit Enhancement**

Entity B, which is issuing $100 million in debt, has a B+ credit rating. As a result, B may be able to issue $100 million in debt at a 12 percent interest rate. However, if B obtains a third-party guarantee from an entity with an AA credit rating, it can issue $100 million in debt at a 6 percent interest rate. Entity B would have to pay the third-party guarantor $20 million to obtain the guarantee.

If B issues $100 million in debt at a 6 percent interest rate because it obtains a guarantee from a third party with an AA credit rating, and if B subsequently defaults on the debt, it is not released from its obligation. Rather, B would be required to reimburse the guarantor. That is, from B's perspective, upon default to the investors in B's debt, the only thing that has changed is the identity of the creditor (i.e., B owes the guarantor instead of the investors).

The guarantee is contractually incorporated into the debt agreement in such a way that any investor that acquires B's debt would be entitled to the guarantee (i.e., the guarantee would be transferred with the debt instrument in transactions among investors).
Example 4-2 (continued)

**Entity B’s Accounting**

If fair value is the measurement attribute for B’s debt, the debt contains two units of accounting: (1) the debt without the guarantee and (2) the guarantee. This is consistent with ASC 825-10-25-13, which states:

For the issuer of a liability issued with an inseparable third-party credit enhancement (for example, debt that is issued with a contractual third-party guarantee), the unit of accounting for the liability measured or disclosed at fair value does not include the third-party credit enhancement. This paragraph does not apply to the holder of the issuer’s credit-enhanced liability or to any of the following financial instruments or transactions:

- A credit enhancement granted to the issuer of the liability (for example, deposit insurance provided by a government or government agency)
- A credit enhancement provided between reporting entities within a consolidated or combined group (for example, between a parent and its subsidiary or between entities under common control).

If B measures the fair value of the debt from the perspective of a market participant that holds the identical item as an asset (i.e., on the basis of the fair value of the debt from the perspective of an investor in B’s debt), an adjustment must be made because there is a factor that applies to the asset that does not apply to B’s liability for the debt. ASC 820-10-35-16D(b) indicates that an entity needs to make an adjustment when the unit of account for the asset is not the same as that for the liability. Further, ASC 820-10-35-16D(b) cites liabilities with third-party credit enhancements (e.g., B’s debt) as an example of a unit of account for which an adjustment is needed. Thus, in measuring the fair value of its debt, B would need to adjust an observed price for the asset to exclude the effect of the third-party guarantee.

**Investor’s Accounting**

If an investor measured its asset for the investment in B’s debt at fair value, it would not exclude the third-party guarantee. Rather, the debt with the inseparable third-party guarantee would be considered as consisting of a single unit of account. The guidance above on separate consideration of a third-party credit enhancement applies only to the issuer (obligor) of the debt.

See Section 4.3.2.2 for further discussion of liabilities with third-party credit enhancements.

### 4.2 Unit of Account Prescribed by ASC 820

**ASC 820-10**

**Level 1 Inputs**

35-44 If a reporting entity holds a position in a single asset or liability (including a position comprising a large number of identical assets or liabilities, such as a holding of financial instruments) and the asset or liability is traded in an active market, the fair value of the asset or liability shall be measured within Level 1 as the product of the quoted price for the individual asset or liability and the quantity held by the reporting entity. That is the case, even if a market’s normal daily trading volume is not sufficient to absorb the quantity held and placing orders to sell the position in a single transaction might affect the quoted price.

As discussed in Section 4.1, ASC 820 specifies one circumstance in which the unit of account is determined for an asset, liability, or equity instrument for fair value measurement or disclosure purposes. In all other instances, entities must determine the unit of account on the basis of other GAAP under which fair value measurement of an item is required (or permitted). ASC 820-10-35-44 specifies the unit of account (and the unit of valuation) for holdings of a single asset or liability traded in an active market. For such assets or liabilities, fair value is measured as “the product of the quoted price for the individual asset or liability and the quantity held by the . . . entity.”
Paragraph C80 of the Basis for Conclusions of FASB Statement 157 (codified in ASC 820) discusses this unit-of-account requirement and states, in part:

This Statement precludes the use of blockage factors and eliminates the exception to $P \times Q$ in the Guides for a financial instrument that trades in an active market (within Level 1). In other words, the unit of account for an instrument that trades in an active market is the individual trading unit. This Statement amends Statements 107, 115, 124, 133, and 140 to remove the similar unit-of-account guidance in those accounting pronouncements, which referred to a fair value measurement using $P \times Q$ for an instrument that trades in any market, including a market that is not active, for example, a thin market (within Level 2). In this Statement, the Board decided not to specify the unit of account for an instrument that trades in a market that is not active.

The FASB addressed inactive markets in subsequently issued guidance. See Section 10.6 for further discussion.

4.3 Allocation to Multiple Units of Account

4.3.1 General

The unit of account (see Section 4.1) represents what is being measured for financial reporting purposes and is related to the level at which assets, liabilities, or equity instruments are aggregated or disaggregated for recognition in the financial statements. With one exception, the unit of account is determined on the basis of guidance in other Codification topics.

The unit of valuation (see Section 5.1) is the grouping of assets, liabilities, or equity instruments for fair value measurement purposes. ASC 820 provides guidance on determining the unit of valuation (see Chapter 5 for more information).

The unit of account may differ from the unit of valuation. Furthermore, even when the unit of account and unit of valuation are the same, the unit of account for fair value measurement purposes may be at a more aggregated level than the unit of account for recognition purposes (e.g., an entity may determine the fair value of a reporting unit to recognize a goodwill impairment loss, in which case the unit of account for the impairment loss is at a more disaggregated level than the unit of account for the fair value measurement, which is the reporting unit). In these circumstances, an entity must allocate the fair value measurement to the individual units of account subject to this measurement. ASC 820 is silent on how to perform this allocation. To do so, an entity must therefore consider the individual facts and circumstances, along with other relevant Codification topics. The Codification topic that specifies the requirement (or ability) to measure an asset, liability, or equity instrument at fair value will generally provide guidance on how to allocate fair value measurements to the appropriate units of account. See Section 4.3.3 for more information.

4.3.2 Financial Assets, Nonfinancial Derivative Assets, Liabilities, and Equity Instruments

The unit of account and unit of valuation are generally the same for financial assets, nonfinancial derivative assets, liabilities, and instruments classified in stockholders’ equity. For such instruments, both the unit of account and the unit of valuation are generally the individual asset, liability, or equity instrument. Therefore, no allocation is necessary for such instruments.
However, as discussed below, there are exceptions to the general principle that the unit of account and unit of valuation are the same for financial assets, nonfinancial derivative assets, liabilities, and instruments classified in stockholders’ equity. Note also that when a derivative instrument must be bifurcated from its host contract, there are two units of account under ASC 815-15 (i.e., the host contract and the embedded derivative) even though the hybrid instrument is considered a freestanding financial instrument. However, when the embedded derivative is measured at fair value, the unit of account and unit of valuation for the embedded derivative are the same.

### 4.3.2.1 Portfolio Valuation Exception for Certain Groups of Assets and Liabilities With Offsetting Risk Positions

One exception to the general principle discussed above applies to the unit of account and unit of valuation for certain financial instruments and nonfinancial derivatives. The exception is available for certain groups of assets and liabilities if an entity (1) manages the group of assets and liabilities on the basis of a net exposure to a market risk (or risks) or counterparty credit risk, (2) provides information on that basis to management, and (3) measures those assets and liabilities at fair value in the statement of financial position. To use this exception, an entity must make an accounting policy decision. Once the accounting policy is established, the entity must consistently apply it from period to period for a particular portfolio. If an entity has made this accounting policy election, the unit of valuation is the entire portfolio of assets and liabilities with offsetting risk exposures. After measuring the fair value of the entire portfolio, the entity must allocate portfolio-based fair value measurement to the individual units of account within the portfolio. Under ASC 820-10-35-18F, such allocations must be performed “on a reasonable and consistent basis using a methodology appropriate in the circumstances.”

**Changing Lanes**

ASU 2018-09 amended ASC 820-10-35-18D to allow a unit of valuation on the basis of a group that includes, in addition to financial assets and financial liabilities, nonfinancial items accounted for as derivatives in accordance with ASC 815, or combinations of these items. Before this amendment, this exception related to the unit of valuation was only allowed for groups of financial assets and financial liabilities with offsetting risk exposures.

See Sections 5.3 and 10.2.8 for more information about this unit-of-valuation exception and how an allocation may be made to the individual units of account for disclosure purposes.

AICPA Technical Q&As Section 6910.34 discusses a similar portfolio-level valuation approach in which an investment company owns a controlling interest in an investee company and holds both equity and debt instruments issued by the investee.

### 4.3.2.2 Liabilities With Third-Party Credit Enhancements

As discussed in Section 10.2.7, an entity may measure the fair value of a liability on the basis of the identical item held as an asset by another party. If the asset includes an inseparable third-party credit enhancement, the unit of account for the liability excludes this credit enhancement. As a result, the valuation premise for the liability is different from the unit of account. Accordingly, an entity must adjust the observed price of the asset so that the fair value measurement of the liability is determined in accordance with its unit of account.
4.3.3 Nonfinancial Assets Other Than Nonfinancial Derivative Assets

ASC 820-10

Valuation Premise for Nonfinancial Assets

35-10E The highest and best use of a nonfinancial asset establishes the valuation premise used to measure the fair value of the asset, as follows:

a. The highest and best use of a nonfinancial asset might provide maximum value to market participants through its use in combination with other assets as a group (as installed or otherwise configured for use) or in combination with other assets and liabilities (for example, a business).
   1. If the highest and best use of the asset is to use the asset in combination with other assets or with other assets and liabilities, the fair value of the asset is the price that would be received in a current transaction to sell the asset assuming that the asset would be used with other assets or with other assets and liabilities and that those assets and liabilities (that is, its complementary assets and the associated liabilities) would be available to market participants.
   2. Liabilities associated with the asset and with the complementary assets include liabilities that fund working capital, but do not include liabilities used to fund assets other than those within the group of assets.
   3. Assumptions about the highest and best use of a nonfinancial asset shall be consistent for all of the assets (for which highest and best use is relevant) of the group of assets or the group of assets and liabilities within which the asset would be used.

b. The highest and best use of a nonfinancial asset might provide maximum value to market participants on a standalone basis. If the highest and best use of the asset is to use it on a standalone basis, the fair value of the asset is the price that would be received in a current transaction to sell the asset to market participants that would use the asset on a standalone basis.

35-11A The fair value measurement of a nonfinancial asset assumes that the asset is sold consistent with the unit of account specified in other Topics (which may be an individual asset). That is the case even when that fair value measurement assumes that the highest and best use of the asset is to use it in combination with other assets or with other assets and liabilities because a fair value measurement assumes that the market participant already holds the complementary assets and associated liabilities.

For nonfinancial assets other than nonfinancial derivative assets, ASC 820 establishes a valuation premise on the basis of the “highest and best use.” As a result, the fair value measurement may encompass a combination of assets and liabilities, including financial instruments. That combination may not be consistent with the unit of account for fair value measurement purposes. Accordingly, an entity will need to allocate the fair value measurement to individual units of account. Other Codification topics will generally specify how to allocate the fair value measurement to individual units of account when either (1) the fair value measurement is performed on the basis of the highest and best use, which is at a level that differs from the unit of account for fair value measurement purposes, or (2) the unit of account for fair value measurement purposes differs from the unit of account for recognition purposes. Below are two situations in which (1) a fair value measurement of nonfinancial assets is performed at a level that is more aggregated than the unit of account for recognition purposes and (2) that fair value amount must therefore be allocated to the units of account. In other situations, entities should determine how to allocate the fair value measurement to the individual units of account by evaluating the facts and circumstances in the context of the guidance in the relevant Codification topic that requires the fair value measurement.

1 For example, the unit of valuation and unit of account for the purpose of testing a film group for impairment may be the film group. However, if an impairment loss is recognized, that loss must be allocated to the films and license agreements within the film group. ASC 926-20-35-19 specifies how to allocate an impairment loss attributable to a film group.
• **Goodwill** — ASC 350 provides guidance on impairment of goodwill. In testing goodwill for impairment under ASC 350, an entity that has not adopted the private company alternative that allows for goodwill impairment testing at the entity level must measure the fair value of the reporting unit to which the goodwill has been allocated.\(^2\) Thus, the reporting unit is the unit of account for fair value measurement purposes. The reporting unit may or may not be the unit of valuation depending on the facts and circumstances. If an impairment of goodwill exists, only goodwill is written down. ASC 350 provides guidance on how to calculate the goodwill impairment loss. As noted in ASC 350-20-35-9, an entity measures the goodwill impairment loss by comparing the implied fair value of the goodwill of the reporting unit with the carrying amount of goodwill. The implied fair value of the goodwill of the reporting unit, which represents only a subset of the overall fair value of the reporting unit, is determined in accordance with ASC 350-20-35-14 through 35-17.

**Changing Lanes**

Under ASC 350, before the amendments made by ASU 2017-04, impairment of goodwill was “the condition that exists when the carrying amount of goodwill exceeds its implied fair value.” The implied fair value of goodwill was determined in the same manner as the amount of goodwill recognized in a business combination. The process of measuring the implied fair value of goodwill was referred to as step 2 of the goodwill impairment test. To perform step 2, an entity was required to “assign the fair value of a reporting unit to all of the assets and liabilities of that unit (including any unrecognized intangible assets) as if the reporting unit had been acquired in a business combination.” Accordingly, performing step 2 sometimes resulted in significant cost and complexity since the “fair value of goodwill can be measured only as a residual and cannot be measured directly.”

ASU 2017-04 simplified the accounting for goodwill impairments by eliminating step 2 from the goodwill impairment test. As amended, ASC 350 states that if “the carrying amount of a reporting unit exceeds its fair value, an impairment loss shall be recognized in an amount equal to that excess, limited to the total amount of goodwill allocated to that reporting unit.” As a result, in measuring the amount of any goodwill impairment loss, an entity no longer needs to allocate the fair value of a reporting unit to individual assets and liabilities to determine the implied fair value of goodwill.

• **Long-lived assets** — ASC 360 requires entities to test long-lived assets for impairment at the asset group level if the assets are held and used and at the disposal group level if the assets are held for sale. Thus, the asset (disposal) group is the unit of account for impairment testing purposes. However, each individual long-lived asset represents an individual unit of account for recognition purposes. Furthermore, the unit of valuation (on the basis of the “highest and best use” concept) could be at a different level than the asset (disposal) group that is being measured at fair value. Thus, if there is an impairment loss (e.g., the fair value of an asset (disposal) group is less than its carrying amount), in accordance with ASC 360-10-35-28, the “loss shall be allocated to the long-lived assets of the group on a pro rata basis using the relative carrying amounts of those assets, except that the loss allocated to an individual long-lived asset of the group shall not reduce the carrying amount of that asset below its fair value whenever that fair value is determinable without undue cost and effort.” In addition, ASC 360 provides guidance on how to allocate the fair value of an asset (disposal) group to financial instruments that are reported at fair value.\(^3\) See also Example 3-1.

\(^2\) ASU 2019-06 extended the accounting alternatives available to private entities to NFP entities.

\(^3\) ASC 360 also provides guidance on situations in which an asset (disposal) group contains other assets that are not long-lived assets (e.g., inventory or receivables).
If the unit of valuation is at a more aggregated level than the unit of account and the Codification topic requiring the fair value measurement does not provide guidance on how to allocate the fair value measurement to the unit (or units) of account, an entity must evaluate the facts and circumstances and use judgment to determine how to appropriately allocate this fair value measurement. In many situations, the use of a relative fair value or another pro rata basis may be appropriate. However, before allocating on such a basis, an entity must ensure that (1) none of the individual assets or liabilities within the group must (or will) be recognized at fair value on an ongoing basis and (2) the allocation would not inappropriately result in the recognition of an asset at more than its fair value. When individual assets or liabilities within a larger group are subsequently measured at fair value, an allocation on the basis of a relative fair value approach will lead to an immediate gain or loss in earnings for the difference between the amount allocated and the then fair value of the asset or liability. This is generally not appropriate. Similarly, if an amount in excess of fair value is allocated to an asset that is not subsequently measured at fair value, the asset may have an immediate impairment loss that must be recognized.
Chapter 5 — Unit of Valuation

5.1 Introduction
As discussed in Chapter 4, the unit of account is the grouping of assets and liabilities that are being measured for financial reporting purposes. The unit of account is generally determined in accordance with the guidance in Codification topics other than ASC 820 and is related to the level of aggregation or disaggregation for recording assets and liabilities.

The unit of valuation (also sometimes referred to as the unit of measurement) is the grouping of assets, liabilities, or equity instruments that are being measured for valuation purposes. The unit of valuation may differ from the unit of account depending on the asset, liability, or equity instrument subject to the fair value measurement. Other Codification topics will generally dictate the unit of account, whereas the unit of valuation is generally addressed in ASC 820. For example, the unit of valuation for nonfinancial assets (other than nonfinancial derivative assets) is based on an asset's highest and best use, which may be on a stand-alone basis or in combination with other assets or other assets and liabilities. An entity may also have the option of grouping certain financial assets, financial liabilities, and nonfinancial items accounted for as derivatives under ASC 815, or a combination of those items, and the portfolio's fair value may be measured on the basis of its net risk position. In this case, the portfolio is the unit of valuation (see Section 5.3).

5.2 Highest and Best Use of Nonfinancial Assets Other Than Nonfinancial Derivative Assets

5.2.1 General

<table>
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<th>ASC 820-10</th>
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The Fair Value Measurement Approach

55-1 The objective of a fair value measurement is to estimate the price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions. A fair value measurement requires a reporting entity to determine all of the following:

a. The particular asset or liability that is the subject of the measurement (consistent with its unit of account)

b. For a nonfinancial asset, the valuation premise that is appropriate for the measurement (consistent with its highest and best use)

c. The principal (or most advantageous) market for the asset or liability

d. The valuation technique(s) appropriate for the measurement, considering the availability of data with which to develop inputs that represent the assumptions that market participants would use when pricing the asset or liability and the level of the fair value hierarchy within which the inputs are categorized.
Highest and Best Use for Nonfinancial Assets

35-10A A fair value measurement of a nonfinancial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

To satisfy the fair value measurement objective, an entity, for nonfinancial assets (other than nonfinancial derivative assets), must determine the fair value on the basis of the valuation premise that is appropriate for the measurement (in a manner consistent with the asset's highest and best use). The unit of valuation (also referred to as the “valuation premise”) for nonfinancial assets (other than nonfinancial derivative assets) is the asset’s highest and best use.

ASC 820-10-20 defines a nonfinancial asset's highest and best use as the “use of a nonfinancial asset by market participants that would maximize the value of the asset or the group of assets and liabilities (for example, a business) within which the asset would be used.” The highest and best use must be determined from a market participant's perspective, regardless of the entity's current or intended use of the nonfinancial asset. The fair value measurement takes into account a market participant's ability to generate economic benefits by putting the asset to its highest and best use or by selling it to another market participant that would do so. However, an entity is not required to perform an exhaustive search to identify the asset's highest and best use and may presume that its current use is the highest and best use if market or other factors do not suggest otherwise.

In determining the highest and best use of a nonfinancial asset, an entity must consider whether the nonfinancial asset's value is maximized through its use either (1) in combination with other assets or other assets and liabilities or (2) on a stand-alone basis. To make such a determination, the entity will need to evaluate the potential use of the asset. Such an evaluation involves consideration of the following:

- Uses of the asset that are physically possible, legally permissible, and financially feasible.
- The entity's current and intended use of the asset.

These concepts are further discussed in Sections 5.2.2 and 5.2.3.

The concept of the highest and best use does not apply to financial assets, nonfinancial derivative assets, liabilities, or instruments classified in stockholders' equity. ASU 2011-04 removed from ASC 820 the application of this concept to financial assets and financial liabilities. Paragraphs BC45 through BC47 of ASU 2011-04 explain the rationale for this decision and state:

BC45. Before the amendments, Topic 820 specified that the concepts of highest and best use and valuation premise applied when measuring the fair value of assets, but it did not distinguish between financial assets and nonfinancial assets.

BC46. In its discussions with the IASB, the Board considered the IASB’s rationale for proposing in its Exposure Draft on fair value measurement that those concepts would not apply to financial assets or to liabilities. The IASB reached that conclusion for the following reasons:

a. Financial assets do not have alternative uses because a financial asset has specific contractual terms and can have a different use only if the characteristics of the financial asset (that is, the contractual terms) are changed. However, a change in characteristics causes that particular asset to become a different asset. The objective of a fair value measurement is to measure the asset that exists at the measurement date.

See Chapter 7 for discussion of the concept of market participants.
b. Even though a reporting entity may be able to change the cash flows associated with a liability by relieving itself of the obligation in different ways, the different ways of doing so are not alternative uses. Moreover, although a reporting entity might have entity-specific advantages or disadvantages that enable it to fulfill a liability more or less efficiently than other market participants, those entity-specific factors do not affect fair value.

c. Those concepts were originally developed within the valuation profession to value nonfinancial assets, such as land.

**BC47.** The Board agreed with the IASB that the concepts of highest and best use and valuation premise are relevant when measuring the fair value of nonfinancial assets and are not relevant when measuring the fair value of financial assets or the fair value of liabilities. The Boards also concluded that those concepts do not apply to instruments classified in shareholders’ equity because those arrangements, similar to financial instruments, typically have specific contractual terms. Paragraphs BC50–BC69 below describe the Boards’ rationale in developing the requirements for measuring the fair value of financial assets and financial liabilities with offsetting positions in market risks and counterparty credit risk.

### 5.2.2 Use in Combination or on a Stand-Alone Basis

<table>
<thead>
<tr>
<th><strong>ASC 820-10</strong></th>
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<tbody>
<tr>
<td><strong>Valuation Premise for Nonfinancial Assets</strong></td>
</tr>
<tr>
<td><strong>35-10E</strong> The highest and best use of a nonfinancial asset establishes the valuation premise used to measure the fair value of the asset, as follows:</td>
</tr>
<tr>
<td>a. The highest and best use of a nonfinancial asset might provide maximum value to market participants through its use in combination with other assets as a group (as installed or otherwise configured for use) or in combination with other assets and liabilities (for example, a business).</td>
</tr>
<tr>
<td>1. If the highest and best use of the asset is to use the asset in combination with other assets or with other assets and liabilities, the fair value of the asset is the price that would be received in a current transaction to sell the asset assuming that the asset would be used with other assets or with other assets and liabilities and that those assets and liabilities (that is, its complementary assets and the associated liabilities) would be available to market participants.</td>
</tr>
<tr>
<td>2. Liabilities associated with the asset and with the complementary assets include liabilities that fund working capital, but do not include liabilities used to fund assets other than those within the group of assets.</td>
</tr>
<tr>
<td>3. Assumptions about the highest and best use of a nonfinancial asset shall be consistent for all of the assets (for which highest and best use is relevant) of the group of assets or the group of assets and liabilities within which the asset would be used.</td>
</tr>
<tr>
<td>b. The highest and best use of a nonfinancial asset might provide maximum value to market participants on a standalone basis. If the highest and best use of the asset is to use it on a standalone basis, the fair value of the asset is the price that would be received in a current transaction to sell the asset to market participants that would use the asset on a standalone basis.</td>
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<tr>
<td><strong>35-11A</strong> The fair value measurement of a nonfinancial asset assumes that the asset is sold consistent with the unit of account specified in other Topics (which may be an individual asset). That is the case even when that fair value measurement assumes that the highest and best use of the asset is to use it in combination with other assets or with other assets and liabilities because a fair value measurement assumes that the market participant already holds the complementary assets and associated liabilities.</td>
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In accordance with ASC 820, the fair value of a nonfinancial asset (other than a nonfinancial derivative asset) may be determined on a combined or stand-alone basis, whichever maximizes the asset’s value. There are various ways in which an asset can be combined either with a group of assets or with other assets or liabilities (such as a business). ASC 820-10-35-10E(a) outlines certain considerations related to situations in which the highest and best use of a nonfinancial asset reflects its use in combination with other assets or with other assets and liabilities.
ASC 820-10-55-3 states that the effect on the fair value measurement of “a nonfinancial asset used in combination with other assets as a group (as installed or otherwise configured for use) or in combination with other assets and liabilities (for example, a business) . . . depends on the circumstances” and gives the following five examples related to this topic:

a. The fair value of the asset might be the same whether the asset is used on a standalone basis or in combination with other assets or with other assets and liabilities. That might be the case if the asset is a business that market participants would continue to operate. In that case, the transaction would involve valuing the business in its entirety. The use of the assets as a group in an ongoing business would generate synergies that would be available to market participants (that is, market participant synergies that, therefore, should affect the fair value of the asset on either a standalone basis or in combination with other assets or with other assets and liabilities).

b. An asset's use in combination with other assets or with other assets and liabilities might be incorporated into the fair value measurement through adjustments to the value of the asset used on a standalone basis. That might be the case if the asset is a machine and the fair value measurement is determined using an observed price for a similar machine (not installed or otherwise configured for use), adjusted for transportation and installation costs so that the fair value measurement reflects the current condition and location of the machine (installed and configured for use).

c. An asset's use in combination with other assets or with other assets and liabilities might be incorporated into the fair value measurement through the market participant assumptions used to measure the fair value of the asset. For example, if the asset is work-in-process inventory that is unique and market participants would convert the inventory into finished goods, the fair value of the inventory would assume that market participants have acquired or would acquire any specialized machinery necessary to convert the inventory into finished goods.

d. An asset's use in combination with other assets or with other assets and liabilities might be incorporated into the valuation technique used to measure the fair value of the asset. That might be the case when using the multiperiod excess earnings method to measure the fair value of an intangible asset because that valuation technique specifically takes into account the contribution of any complementary assets and the associated liabilities in the group in which such an intangible asset would be used.

e. In more limited situations, when a reporting entity uses an asset within a group of assets, the reporting entity might measure the asset at an amount that approximates its fair value when allocating the fair value of the asset group to the individual assets of the group. That might be the case if the valuation involves real property and the fair value of improved property (that is, an asset group) is allocated to its component assets (such as land and improvements).

In a speech at the 2009 AICPA National Conference on Current SEC and PCAOB Developments, Evan Sussholz, then a professional accounting fellow in the SEC’s Office of the Chief Accountant, addressed the determination of the highest and best use of a nonfinancial asset. Mr. Sussholz stated, in part:

Question #2: What is the highest and best use for the asset?

To answer this question, a reporting entity should identify all of the potential uses of the asset within each potential exit market and determine if the value of the asset would be maximized by using the asset on a standalone basis (that is, an in-exchange valuation premise) or in conjunction with other assets (that is, an in-use valuation premise).

For example, market participants may derive value from a customer related intangible asset through its use as a stand-alone asset such as renting the customer list to third parties. Alternatively, a market participant may derive value from a customer related intangible asset through its use in combination with other assets such as trademarks, fixed assets, and goodwill. The reporting entity should determine the asset's highest and best use based on the use that maximized the fair value of the individual asset or group of assets in which the asset is being used.

The highest and best use of a nonfinancial asset (other than a nonfinancial derivative asset) might result in maximum value for market participants on a stand-alone basis. If the fair value is determined on a stand-alone basis, the fair value of the asset is the price that would be received in a current transaction to sell the asset to market participants that would use the asset on a stand-alone basis.
Chapter 5 — Unit of Valuation

ASC 820-10-35-11A clarifies that regardless of whether the highest and best use of a nonfinancial asset is on a combined or stand-alone basis, the fair value of the nonfinancial asset must be measured on the basis of a sale of the nonfinancial asset that is consistent with its unit of account, as specified in other Codification topics. The reason for this requirement is that when fair value is determined under an assumption that the highest and best use of the asset is in combination with other assets or with other assets and liabilities, it is assumed that “the market participant already holds the complementary assets and associated liabilities.”

5.2.3 Potential Uses of the Asset

5.2.3.1 General

In determining the valuation premise (i.e., the highest and best use of a nonfinancial asset), an entity must consider the asset’s potential uses. The entity then uses this information to determine whether the nonfinancial asset’s highest and best use is on a combined or stand-alone basis.

5.2.3.2 Physically Possible, Legally Permissible, and Financially Feasible

In determining the highest and best use of a nonfinancial asset (other than a nonfinancial derivative asset), an entity must assess the following two characteristics:

- **Physical possibility** — ASC 820 requires an entity to consider the physical characteristics of the asset. In doing so, an entity must take certain considerations into account, including the asset’s location or size and whether its physical characteristics allow for potential alternative uses that would maximize its value from a market-participant perspective. The highest and best use of a nonfinancial asset should not represent a use that is physically impossible. For example, it would not be physically possible to relocate a parcel of land. It may, however, be physically possible to relocate certain other types of nonfinancial assets, such as machinery or equipment. However, an entity would determine the cost of such relocation (including any installation or other relevant costs) in determining whether it would maximize value to a market participant. See further discussion of financial feasibility below.

- **Legal permissibility** — ASC 820 requires an entity to consider the legally permissible uses of a nonfinancial asset to determine fair value from a market-participant perspective. The highest and best use of a nonfinancial asset should represent a use that is legally permissible. The consideration of legal permissibility takes into account whether a particular use is legally permissible both currently and in the future. That is, an entity is not necessarily precluded
from considering legally permissible uses in the future. For example, market participants may consider the possibility that current legal restrictions, such as zoning ordinances, may change in the future and adjust the pricing of an asset accordingly. Therefore, the fair value measurement should take into account the risk of uncertainty that legal restrictions may change and the costs a market participant would incur to transform the asset's use. Such costs may include, but are not limited to, costs imposed by a governmental entity or regulator. See Example 5-1 below for a related illustration.

In evaluating physically possible and legally permissible uses of a nonfinancial asset (other than a nonfinancial derivative asset), entities must consider “financial feasibility” from a market-participant perspective in accordance with ASC 820-10-35-10B(c). As part of this evaluation, an entity determines whether the asset would generate adequate investment returns (e.g., cash flows) that market participants would demand to put the asset to that use. In performing this evaluation, an entity effectively would need to assess the return on invested capital, including the risks and uncertainties related to both the investment returns and the potential costs of generating such returns. Further, an entity would have to consider the targeted return on market participants’ invested capital.

Example 5-1

Zoning Requirements That Apply to a Parcel of Land

Entity A holds a parcel of land that is zoned for residential use as of the measurement date; however, the highest and best use of the land is commercial use. Although A may consider the possibility that the land could be rezoned at some point in the future when performing its fair value measurement, it would also need to consider the risks of rezoning (e.g., the risk that the land might not be rezoned) and the cost of transforming the asset. Depending on the cost of transforming the asset, the fair value of A’s land would be between the residential value and the commercial value.

5.2.3.3 Current or Intended Use

ASC 820-10

Highest and Best Use for Nonfinancial Assets

35-10C Highest and best use is determined from the perspective of market participants, even if the reporting entity intends a different use. However, a reporting entity’s current use of a nonfinancial asset is presumed to be its highest and best use unless market or other factors suggest that a different use by market participants would maximize the value of the asset.

35-10D To protect its competitive position, or for other reasons, a reporting entity may intend not to use an acquired nonfinancial asset actively, or it may intend not to use the asset according to its highest and best use. For example, that might be the case for an acquired intangible asset that the reporting entity plans to use defensively by preventing others from using it. Nevertheless, the reporting entity shall measure the fair value of a nonfinancial asset assuming its highest and best use by market participants.
Nonfinancial assets should be valued on the basis of the assumptions market participants would use. In performing this valuation, a market participant would consider its ability to generate economic benefits by putting the asset to its highest and best use or by selling it to another market participant that would do so. Further, the assessment should be from a market participant’s perspective, even if the entity determines that it would use the asset differently. In other words, an entity should consider a market participant’s, but not its own, assumptions regarding the use or disposition of a nonfinancial asset. While a market participant could use the asset in a different way than the entity does, if no market or other factors suggest a different use by market participants, the current use of the asset by the entity is presumed to be its highest and best use.

ASC 820-10-35-10D provides guidance on nonfinancial assets whose intended use differs from their highest and best use (e.g., defensive intangible assets). Even if they are intangible rather than tangible, these assets must still be measured at fair value in accordance with ASC 820. That is, even if an entity does not intend to use a nonfinancial asset or intends to use it in a way other than its highest and best use, the entity must measure the asset at fair value under ASC 820 on the basis of its highest and best use.

For example, an entity may decide not to use the acquired trade name of a competitor but may intend to keep the name (rather than sell it) solely to prevent others from using it. In this case, the asset is determined to have value to the acquirer, albeit this value is defensive (i.e., because others are prevented from using the asset). When measuring the fair value of a defensive intangible asset in accordance with ASC 820, an acquirer should assume its highest and best use by market participants.

### 5.2.3.4 ASC 820 Examples

<table>
<thead>
<tr>
<th>ASC 820-10</th>
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<tbody>
<tr>
<td><strong>Case B: Land</strong></td>
</tr>
<tr>
<td><strong>55-30</strong> A reporting entity acquires land in a business combination. The land is currently developed for industrial use as a site for a factory. The current use of land is presumed to be its highest and best use unless market or other factors suggest a different use. Nearby sites have recently been developed for residential use as sites for high-rise apartment buildings. On the basis of that development and recent zoning and other changes to facilitate that development, the reporting entity determines that the land currently used as a site for a factory could be developed as a site for residential use (that is, for high-rise apartment buildings) because market participants would take into account the potential to develop the site for residential use when pricing the land.</td>
</tr>
<tr>
<td><strong>55-31</strong> The highest and best use of the land would be determined by comparing both of the following:</td>
</tr>
<tr>
<td>a. The value of the land as currently developed for industrial use (that is, the land would be used in combination with other assets, such as the factory, or with other assets and liabilities)</td>
</tr>
<tr>
<td>b. The value of the land as a vacant site for residential use, taking into account the costs of demolishing the factory and other costs (including the uncertainty about whether the reporting entity would be able to convert the asset to the alternative use) necessary to convert the land to a vacant site (that is, the land is to be used by market participants on a standalone basis).</td>
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The highest and best use of the land would be determined on the basis of the higher of those values. In situations involving real estate appraisal, the determination of highest and best use might take into account factors relating to the factory operations, including its assets and liabilities.
Case C: In-Process Research and Development Project

55-32 A reporting entity acquires an in-process research and development project in a business combination. The reporting entity does not intend to complete the project. If completed, the project would compete with one of its own projects (to provide the next generation of the reporting entity’s commercialized technology). Instead, the reporting entity intends to hold (that is, lock up) the project to prevent its competitors from obtaining access to the technology. In doing this, the project is expected to provide defensive value, principally by improving the prospects for the reporting entity’s own competing technology. To measure the fair value of the project at initial recognition, the highest and best use of the project would be determined on the basis of its use by market participants. For example:

a. The highest and best use of the in-process research and development project would be to continue development if market participants would continue to develop the project and that use would maximize the value of the group of assets or of assets and liabilities in which the project would be used (that is, the asset would be used in combination with other assets or with other assets and liabilities). That might be the case if market participants do not have similar technology, either in development or commercialized. The fair value of the project would be measured on the basis of the price that would be received in a current transaction to sell the project, assuming that the in-process research and development would be used with its complementary assets and the associated liabilities and that those assets and liabilities would be available to market participants.

b. The highest and best use of the in-process research and development project would be to cease development if, for competitive reasons, market participants would lock up the project and that use would maximize the value of the group of assets or of assets and liabilities in which the project would be used. That might be the case if market participants have technology in a more advanced stage of development that would compete with the project if completed and the project would be expected to improve the prospects for their own competing technology if locked up. The fair value of the project would be measured on the basis of the price that would be received in a current transaction to sell the project, assuming that the in-process research and development would be used (that is, locked up) with its complementary assets and the associated liabilities and that those assets and liabilities would be available to market participants.

c. The highest and best use of the in-process research and development project would be to cease development if market participants would discontinue its development. That might be the case if the project is not expected to provide a market rate of return if completed and would not otherwise provide defensive value if locked up. The fair value of the project would be measured on the basis of the price that would be received in a current transaction to sell the project on its own (which might be zero).

5.3 Certain Groups of Assets and Liabilities With Offsetting Risk Positions

Application to Financial Assets and Financial Liabilities With Offsetting Positions in Market Risks or Counterparty Credit Risk

35-18D A reporting entity that holds a group of financial assets and financial liabilities is exposed to market risks (that is, interest rate risk, currency risk, or other price risk) and to the credit risk of each of the counterparties. If the reporting entity manages that group of financial assets and financial liabilities on the basis of its net exposure to either market risks or credit risk, the reporting entity is permitted to apply an exception to this Topic for measuring fair value. That exception permits a reporting entity to measure the fair value of a group of financial assets and financial liabilities on the basis of the price that would be received to sell a net long position (that is, an asset) for a particular risk exposure or paid to transfer a net short position (that is, a liability) for a particular risk exposure in an orderly transaction between market participants at the measurement date under current market conditions. Accordingly, a reporting entity shall measure the fair value of the group of financial assets and financial liabilities consistently with how market participants would price the net risk exposure at the measurement date.
Pending Content (Transition Guidance: ASC 105-10-65-5)

35-18D A reporting entity that holds a group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items is exposed to market risks (that is, interest rate risk, currency risk, or other price risk) and to the credit risk of each of the counterparties. If the reporting entity manages that group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items on the basis of its net exposure to either market risks or credit risk, the reporting entity is permitted to apply an exception to this Topic for measuring fair value. That exception permits a reporting entity to measure the fair value of a group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items on the basis of the price that would be received to sell a net long position (that is, an asset) for a particular risk exposure or paid to transfer a net short position (that is, a liability) for a particular risk exposure in an orderly transaction between market participants at the measurement date under current market conditions. Accordingly, a reporting entity shall measure the fair value of the group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items consistently with how market participants would price the net risk exposure at the measurement date.

As discussed in Section 4.3.2, the unit of valuation for financial assets, nonfinancial derivative assets, all liabilities, and equity instruments is generally the individual instrument, which is generally also its unit of account under other GAAP. As stated in Section 5.2.1, the concept of the highest and best use does not apply to financial assets, nonfinancial derivative assets, liabilities, or instruments classified in stockholders’ equity.

An exception to ASC 820’s general principles related to the unit of valuation for financial assets and liabilities is available for groups of financial assets and financial liabilities if an entity (1) manages the group of assets and liabilities on the basis of net exposure to a market risk (or risks) or counterparty credit risk, (2) provides information on that basis to management, and (3) measures those assets and liabilities at fair value in the statement of financial position. ASC 820-10-35-18D discusses this exception and states, in part:

That exception permits a reporting entity to measure the fair value of a group of financial assets [and financial liabilities] on the basis of the price that would be received to sell a net long position (that is, an asset) for a particular risk exposure or paid to transfer a net short position (that is, a liability) for a particular risk exposure in an orderly transaction between market participants at the measurement date under current market conditions. Accordingly, [an entity that elects this exception should] measure the fair value of the group of financial assets [and financial liabilities] consistently with how market participants would price the net risk exposure at the measurement date.\(^2\)

An entity must elect the exception as an accounting policy and consistently apply it from period to period for a particular portfolio. See Section 10.2.8.1 for further discussion of the application of this portfolio valuation exception, including its application to nonfinancial derivatives as a result of the amendments made by ASU 2018-09.

\(^2\) See Section 10.4.4 for discussion of the use of mid-market pricing as a practical expedient.
5.4 Liabilities and Instruments Classified in Equity

ASC 820-10

**Application to Liabilities and Instruments Classified in a Reporting Entity's Shareholders' Equity**

35-16 A fair value measurement assumes that a financial or nonfinancial liability or an instrument classified in a reporting entity's shareholders' equity (for example, equity interests issued as consideration in a business combination) is transferred to a market participant at the measurement date. The transfer of a liability or an instrument classified in a reporting entity's shareholders' equity assumes the following: . . .

b. A liability would remain outstanding and the market participant transferee would be required to fulfill the obligation. The liability would not be settled with the counterparty or otherwise extinguished on the measurement date.

c. An instrument classified in a reporting entity's shareholders' equity would remain outstanding and the market participant transferee would take on the rights and responsibilities associated with the instrument. The instrument would not be cancelled or otherwise extinguished on the measurement date.

When a liability or an instrument classified within an entity's stockholders' equity is measured at fair value, it is assumed that the liability or equity instrument is transferred to a market participant on the measurement date. Specifically, ASC 820-10-35-16 requires entities measuring the fair value of a liability to assume that the liability remains outstanding and is transferred to a market participant transferee that “would be required to fulfill the obligation.” Similarly, entities must assume that an “instrument classified in . . . shareholders' equity would remain outstanding and the market participant transferee would take on the rights and responsibilities associated with the instrument.” A liability being measured at fair value would not be assumed to be settled, and an instrument classified in shareholders' equity would not be assumed to be canceled or otherwise extinguished. However, ASC 820-10-35-16B points out that “[w]hen a quoted price for the transfer of an identical or a similar liability or [an entity's own equity instrument] is not available and the identical item is held by another party as an asset, a reporting entity shall measure the fair value of the liability or [the entity's own] equity instrument from the perspective of a market participant that holds the identical item as an asset at the measurement date.” See Section 10.2.7 for further discussion of the fair value measurement of liabilities and equity instruments.
Chapter 6 — The Principal or Most Advantageous Market

6.1 General

ASC 820-10

The Transaction

35-5 A fair value measurement assumes that the transaction to sell the asset or transfer the liability takes place either:

   a. In the principal market for the asset or liability
   b. In the absence of a principal market, in the most advantageous market for the asset or liability.

35-5A A reporting entity need not undertake an exhaustive search of all possible markets to identify the principal market or, in the absence of a principal market, the most advantageous market, but it shall take into account all information that is reasonably available. In the absence of evidence to the contrary, the market in which the reporting entity normally would enter into a transaction to sell the asset or to transfer the liability is presumed to be the principal market or, in the absence of a principal market, the most advantageous market.

35-6 If there is a principal market for the asset or liability, the fair value measurement shall represent the price in that market (whether that price is directly observable or estimated using another valuation technique), even if the price in a different market is potentially more advantageous at the measurement date.

35-6A The reporting entity must have access to the principal (or most advantageous) market at the measurement date. Because different entities (and businesses within those entities) with different activities may have access to different markets, the principal (or most advantageous) market for the same asset or liability might be different for different entities (and businesses within those entities). Therefore, the principal (or most advantageous) market (and thus, market participants) shall be considered from the perspective of the reporting entity, thereby allowing for differences between and among entities with different activities.

35-6B Although a reporting entity must be able to access the market, the reporting entity does not need to be able to sell the particular asset or transfer the particular liability on the measurement date to be able to measure fair value on the basis of the price in that market.
The Fair Value Measurement Approach

55-1 The objective of a fair value measurement is to estimate the price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions. A fair value measurement requires a reporting entity to determine all of the following:

a. The particular asset or liability that is the subject of the measurement (consistent with its unit of account)
b. For a nonfinancial asset, the valuation premise that is appropriate for the measurement (consistent with its highest and best use)
c. The principal (or most advantageous) market for the asset or liability
d. The valuation technique(s) appropriate for the measurement, considering the availability of data with which to develop inputs that represent the assumptions that market participants would use when pricing the asset or liability and the level of the fair value hierarchy within which the inputs are categorized.

Underlying the fair value measurement objective in ASC 820 is the concept that an entity would transact in the principal market for the asset, liability, or equity instrument subject to the fair value measurement, or in the absence of a principal market, the most advantageous market. The determination of the principal (or most advantageous) market for an asset, liability, or equity instrument can affect the fair value measurement since the exit price may differ from market to market. (See Sections 6.2 and 6.3 for a discussion of the concepts of the principal market and most advantageous market.) In evaluating which of two or more accessible markets is the principal (or most advantageous) market, an entity must apply the market-participant approach.

6.1.1 Access Considerations

For a market to represent the principal (or most advantageous) market, an entity must have access to it as of the measurement date. However, ASC 820-10-35-6B indicates that an entity is not required “to be able to sell the particular asset or transfer the particular liability on the measurement date” in that market. An example of a situation in which an entity has access to a market but is unable to sell an asset in that market is one in which an entity is precluded from transferring an asset as of the measurement date. See Section 10.2.2.2 for further discussion of restrictions on the sale or use of an asset.

In a speech at the 2015 AICPA National Conference on Current SEC and PCAOB Developments, Kris Shirley, then a professional accounting fellow in the SEC’s Office of the Chief Accountant, outlined certain factors that may prevent an entity from accessing a particular price within a market as of the measurement date:

- The fair value measurement guidance also indicates a reporting entity must have access to the principal or most advantageous market at the measurement date. [Footnote omitted] If the reporting entity cannot transact in a particular market on the measurement date, then that market may not constitute the principal or most advantageous market.

- Being able to transact in a market on the measurement date, I would like to point out, is something that may need to be considered even when relying on observable pricing as an input into a fair value measurement. An entity may need to consider any different characteristics associated with its asset or liability being measured at fair value and the observable pricing. Different characteristics may prevent an entity from accessing the observable market on the measurement date at the price observed within the market and may lead to a different principal or most advantageous market for fair value measurement purposes.
Some observations regarding common characteristics that may prevent an entity from accessing a particular price within a market include, but are not limited to, the following:

- a reporting entity's need to transform the asset or liability in some way to match the asset or liability in the observable market;
- restrictions that may be unique to the reporting entity's asset or liability that are not embedded in the asset or liability in the observable market; and
- marketability or liquidity differences between the asset or liability in the observable market relative to the reporting entity's asset or liability.

A reporting entity may not be precluded from using observable prices from a particular market as one input into its fair value measurement (even if the market does not constitute the principal market); however, an entity may need to make appropriate adjustments to the fair value measurement for any differences in the characteristics of the asset or liability being measured and the price observed within a market. For example, an entity that is measuring the fair value of a loan may look to the securitization market when measuring the value of the loan, but would need to make appropriate adjustments to the observed securities prices to reflect the fact that the loan has not been securitized as of the measurement date.

For purposes of determining the reporting entity's principal or most advantageous market, I would consider starting with the initial transaction. There may be situations when the market in which the initial transaction occurs is different than the principal or most advantageous market. In those situations, a reporting entity may need to consider whether it is able to access the principal or most advantageous market for the asset or liability on the measurement date.

Note that an entity would evaluate market access from its own perspective rather than from a market-participant perspective. Example 4 in ASC 820-10-55-42 through 55-45A illustrates a scenario in which two entities measure the same instrument differently because each entity identifies a different principal market on the basis of its own activities. For further discussion, see Section 6.5.

### 6.1.2 Market-Participant Considerations

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<td><strong>The Transaction</strong></td>
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<td><strong>35-5A</strong></td>
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<tr>
<td><strong>35-6C</strong></td>
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As noted in ASC 820-10-35-6C above, an entity needs to determine the fair value of an asset, liability, or equity instrument from a market-participant perspective. However, ASC 820-10-35-6C also points out that there may be situations in which “there is no observable market to provide pricing information about the sale of an asset or the transfer of a liability at the measurement date.” When an observable market for an asset does not exist, an entity must develop a hypothetical (assumed) transaction as of the measurement date in accordance with the fair value objective in ASC 820. In doing so, an entity must consider characteristics of potential market participants (the entity does not have to identify specific market participants) that would transact for the asset and, in the case of nonfinancial assets, maximize the asset's value. An entity may need to make adjustments to reflect factors specific to an asset or liability (e.g., the location and condition of a nonfinancial asset, synergies specific to the entity
but not available to market participants, growth rates, and risk adjustments). These adjustments would be made on the basis of market-participant assumptions. See Section 10.2.2.1 for further discussion of the characteristics of an asset or liability that market participants would consider in pricing the asset or liability as of the measurement date.

### 6.1.3 Different Markets Within a Reporting Entity

The principal (or most advantageous) market for the same asset, liability, or equity instrument might vary from entity to entity (and from business to business within an entity) given that entities with different activities may have access to different markets. The analysis of the principal (or most advantageous) market does not differ for subsidiaries. A subsidiary identifies its principal (or most advantageous) market when it measures the fair value of assets and liabilities by considering both of the following:

- Its own perspective on identifying markets that it can access.
- Market participants’ perspectives on assessing which of two or more accessible markets is the principal (or most advantageous) market.

An entity should consider all markets that can be accessed through its parent or related subsidiary, taking into account any restrictions that prohibit the entity from transferring the asset or liability to its parent or related subsidiary, including excessive transportation costs. That is, it should not be assumed that a subsidiary can access a given market through its parent or related subsidiary if there are legal restrictions against (1) transferring the asset to that parent or subsidiary or (2) selling the asset in that market. However, legal restrictions are not the only barriers to accessing a given market. An entity must consider other relevant circumstances, such as cost-prohibitive import tariffs or other transportation costs that make the likelihood of accessing a different market less than reasonably possible. A subsidiary should also consider the guidance in ASC 820-10-35-5A, which indicates that an entity does not need to perform “an exhaustive search of all possible markets” and that, in the absence of information to the contrary, it is presumed that the market in which the transaction occurs would be its principal market. See Example 6-4 for a scenario involving multiple principal markets in an entity’s consolidated financial statements.

### 6.2 The Principal Market

**ASC 820-10 — Glossary**

**Principal Market**

The market with the greatest volume and level of activity for the asset or liability.

An entity identifies the principal market for an asset, liability, or equity instrument by first identifying all markets that it can access to sell the asset or transfer the liability or equity instrument. The principal market is the market that, from a market-participant perspective, has the greatest volume or level of activity. While there will generally be a principal market, in the absence of a principal market, the entity identifies the most advantageous market, which is the market that maximizes the fair value of the asset or minimizes the fair value of the liability.
The glossary in ASC 820-10-20 gives several examples of markets that could be the principal market for an entity:

**ASC 820-10 — Glossary**

**Brokered Market**
A market in which brokers attempt to match buyers with sellers but do not stand ready to trade for their own account. In other words, brokers do not use their own capital to hold an inventory of the items for which they make a market. 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. Brokered markets include electronic communication networks, in which buy and sell orders are matched, and commercial and residential real estate markets.

**Dealer Market**
A market in which dealers stand ready to trade (either buy or sell for their own account), thereby providing liquidity by using their capital to hold an inventory of the items for which they make a market. Typically, bid and ask prices (representing the price at which the dealer is willing to buy and the price at which the dealer is willing to sell, respectively) are more readily available than closing prices. Over-the-counter markets (for which prices are publicly reported by the National Association of Securities Dealers Automated Quotations systems or by OTC Markets Group Inc.) are dealer markets. For example, the market for U.S. Treasury securities is a dealer market. Dealer markets also exist for some other assets and liabilities, including other financial instruments, commodities, and physical assets (for example, used equipment).

**Exchange Market**
A market in which closing prices are both readily available and generally representative of fair value. An example of such a market is the New York Stock Exchange.

**Principal-to-Principal Market**
A market in which transactions, both originations and resales, are negotiated independently with no intermediary. Little information about those transactions may be made available publicly.

An entity is not required to perform an exhaustive search to identify all markets that could potentially be the principal market. In fact, unless contradictory evidence exists, it is presumed that the market in which the entity normally transacts is the principal market for the asset or liability. This concept is discussed in paragraph BC23 of **ASU 2011-04**, which states:

In addition, the Boards concluded that a reporting entity normally enters into transactions in the principal market for the asset or liability (that is, the most liquid market, assuming that the reporting entity can access that market). As a result, the Boards decided to specify that a reporting entity can use the price in the market in which it normally enters into transactions, unless there is evidence that the principal market and that market are not the same. Consequently, a reporting entity does not need to perform an exhaustive search for markets that might have more activity for the asset or liability than the market in which that reporting entity normally enters into transactions. Thus, the amendments address practical concerns about the costs of searching for the market with the greatest volume and level of activity for the asset or liability.
In a speech at the 2009 AICPA National Conference on Current SEC and PCAOB Developments, Evan Sussholz, then a professional accounting fellow in the SEC's Office of the Chief Accountant, addressed questions for entities to consider in determining the principal (or most advantageous) market. Specifically, Mr. Sussholz stated:

Question #1: What are the potential exit markets for an asset and what is the asset's principal or most advantageous market?

For an actively-traded financial asset, the principal (or most advantageous) market may simply be an exchange such as the NYSE or NASDAQ. However, for many assets such as non-financial assets, determining the principal (or most advantageous) market could be more difficult as the market for these assets may be inactive or non-existent and observable pricing information may not be readily available. Furthermore, certain defining characteristics of individual markets may have an impact on the timing and ultimate selling price of an asset. When performing an analysis of each potential exit market, it may be important for a reporting entity to understand the following:

- Is the market for the asset active, inactive, or has it recently become inactive?
- Are there distinct groups of potential market participants in that market such as strategic buyers and financial buyers? Within these groups, are there clusters of potential participants (i.e. small vs. large, profitable vs. unprofitable, etc.)
- What is the competitive nature of the market (i.e. perfect competition, monopolistic or oligopolistic competition, fragmented markets)?

To begin our example, let’s assume that there are two potential exit markets for the customer related intangible asset being measured including the customer list broker market and the mergers and acquisitions (M&A) market. Each of these markets has defining characteristics such as level of activity, groups of market participants, and differing levels of competitiveness. While a reporting entity may be able to obtain some pricing information from both markets, significant adjustments may be required to determine an estimated selling pricing for the specific customer related intangible asset being measured.

In most cases, the principal market is the same as the most advantageous market. Entities would generally change markets, unless impractical, if there was a more advantageous market. However, if there is a principal market, the fair value measurement should represent the fair value in that market even if the fair value in a different market is potentially more advantageous.

6.3 Most Advantageous Market

<table>
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<tr>
<td><strong>Most Advantageous Market</strong></td>
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<tr>
<td>The market that maximizes the amount that would be received to sell the asset or minimizes the amount that would be paid to transfer the liability, after taking into account transaction costs and transportation costs.</td>
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</table>

The concept of a most advantageous market is relevant only when there is no principal market for an asset, liability, or equity instrument. In identifying the most advantageous market, an entity must consider both its own and market participants’ perspectives. An entity considers its own perspective in identifying markets that it can access. An entity then considers market-participant perspectives in assessing which of two or more accessible markets is the most advantageous market. Thus, the assessment and considerations in Section 6.2 that pertain to determining the principal market are also relevant in an entity’s determination of the most advantageous market. Note that while an entity considers both transaction and transportation costs in determining the most advantageous market, transaction costs are not included in a fair value measurement under ASC 820 (as discussed in Section 10.2.5.3).
6.4 Changes in the Principal or Most Advantageous Market

Events that could indicate a change in the principal (or most advantageous) market include (1) a significant change in market conditions, (2) the development of a new market, and (3) the entity’s obtaining access to a market to which it previously did not have access. An entity must evaluate all facts and circumstances in determining whether there has been a change in the principal (or most advantageous) market. Events could lead to a conclusion that there is no longer a principal market for an asset in which an entity would have to identify the most advantageous market. Examples 6-2 and 6-3 illustrate scenarios in which potential changes in the principal (or most advantageous) market have occurred.

6.5 Examples

Example 4 in ASC 820-10-55-42 through 55-45A illustrates a scenario in which two entities may measure the same instrument differently because each entity identifies a different principal (or most advantageous) market.

<table>
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<tr>
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<tr>
<td><strong>Example 4: Level 1 Principal (or Most Advantageous) Market</strong></td>
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<tr>
<td><strong>55-42</strong> Example 4 illustrates the use of Level 1 inputs to measure the fair value of an asset that trades in different active markets at different prices.</td>
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<tr>
<td><strong>55-43</strong> An asset is sold in two different active markets at different prices. A reporting entity enters into transactions in both markets and can access the price in those markets for the asset at the measurement date. In Market A, the price that would be received is $26, transaction costs in that market are $3, and the costs to transport the asset to that market are $2 (that is, the net amount that would be received is $21). In Market B, the price that would be received is $25, transaction costs in that market are $1, and the costs to transport the asset to that market are $2 (that is, the net amount that would be received in Market B is $22).</td>
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<tr>
<td><strong>55-44</strong> If Market A is the principal market for the asset (that is, the market with the greatest volume and level of activity for the asset), the fair value of the asset would be measured using the price that would be received in that market, after taking into account transportation costs ($24).</td>
</tr>
<tr>
<td><strong>55-45</strong> If neither market is the principal market for the asset, the fair value of the asset would be measured using the price in the most advantageous market. The most advantageous market is the market that maximizes the amount that would be received to sell the asset after taking into account transaction costs and transportation costs (that is, the net amount that would be received in the respective markets).</td>
</tr>
<tr>
<td><strong>55-45A</strong> Because the reporting entity would maximize the net amount that would be received for the asset in Market B ($22), the fair value of the asset would be measured using the price in that market ($25), less transportation costs ($2), resulting in a fair value measurement of $23. Although transaction costs are taken into account when determining which market is the most advantageous market, the price used to measure the fair value of the asset is not adjusted for those costs (although it is adjusted for transportation costs).</td>
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</table>
Further, Example 5 in ASC 820-10-55-46 through 55-49 illustrates a scenario in which an entity’s principal entry markets differ from its principal exit markets.

**ASC 820-10**

*Example 5: Transaction Prices and Fair Value at Initial Recognition — Interest Rate Swap at Initial Recognition*

**55-46** This Topic (see paragraphs 820-10-30-3 through 30-3A) clarifies that in many cases the transaction price, that is, the price paid (received) for a particular asset (liability), will represent the fair value of that asset (liability) at initial recognition, but not presumptively. This Example illustrates when the price in a transaction involving a derivative instrument might (and might not) equal the fair value of the instrument at initial recognition.

**55-47** Entity A (a retail counterparty) enters into an interest rate swap in a retail market with Entity B (a dealer) for no initial consideration (that is, the transaction price is zero). Entity A can access only the retail market. Entity B can access both the retail market (that is, with retail counterparties) and the dealer market (that is, with dealer counterparties).

**55-48** From the perspective of Entity A, the retail market in which it initially entered into the swap is the principal market for the swap. If Entity A were to transfer its rights and obligations under the swap, it would do so with a dealer counterparty in that retail market. In that case, the transaction price (zero) would represent the fair value of the swap to Entity A at initial recognition, that is, the price that Entity A would receive to sell or pay to transfer the swap in a transaction with a dealer counterparty in the retail market (that is, an exit price). That price would not be adjusted for any incremental (transaction) costs that would be charged by that dealer counterparty.

**55-49** From the perspective of Entity B, the dealer market (not the retail market) is the principal market for the swap. If Entity B were to transfer its rights and obligations under the swap, it would do so with a dealer in that market. Because the market in which Entity B initially entered into the swap is different from the principal market for the swap, the transaction price (zero) would not necessarily represent the fair value of the swap to Entity B at initial recognition.

Below are four additional examples illustrating the determination of the principal (or most advantageous) market.

**Example 6-1**

*Multiple Markets in Different Countries*

Entity A, a global commodity company that connects commodity buyers around the world, has a commodity sourcing strategy for customers located in Country Z. The commodities are recognized at fair value by A.

As part of A’s commodity sourcing strategy, a wholly owned subsidiary of A that is domiciled in Country Y buys the commodities in Country Y and executes intercompany sales of the commodities to a wholly owned subsidiary in Country Z. Country Z faces certain heightened economic risks stemming from uncertainty in its access to foreign currency in the amounts necessary to satisfy large-scale contracts as well as other limitations that have resulted from economic sanctions placed on it by other countries.

Commodities are delivered to Country Z through Country Y, which is adjacent to Country Z. There is an active market in Country Y that can rapidly absorb significant amounts of a particular commodity. Because A readily has access to, and the ability to transact in, the active market in Country Y, it can sell the commodity to buyers in Country Z after incurring insignificant transportation costs. Entity A may also purchase the commodity in Country Z; however, the market in Country Z is not active. As a result, the commodities sold to customers in Country Z are purchased in Country Y.
Example 6-1 (continued)

Entity A should assess its principal market for the commodity from its own perspective. Only in the absence of a principal market may A look to prices in the most advantageous market. Two entities may measure the same commodity differently because each entity identifies a different principal market on the basis of its own activities.

Entity A purchases and stores in Country Y the commodities that it sells to Country Z. Although A may purchase quantities of the commodity in Country Z to sell to customers in that country, A should look to Country Y when determining the fair value of the commodities sold to customers in Country Z, given the presence of an active market in Country Y (i.e., the market with the greatest level of activity and volume exists for the commodity). Although there is a market for the commodity in Country Z, it could not represent the market in the determination of the fair value of the commodity, since there is a principal market for the commodity in Country Y.

Example 6-2

Purchases on Multiple Markets

Entity B is a global commodity company that holds commodities in several different storage facilities in different geographical regions. These commodities are carried at fair value.

Entity B holds a certain quantity of commodities in Country W that it expects to sell to customers in that country. Country W has an active market for the commodities that can rapidly absorb significant amounts of them, and B readily has access to, as well as the ability to transact in, that market. While the market for the commodity in Country W is considered active and is the market in which B sells the commodity, in certain instances, B will sell the commodities held in storage in Country W on the F Exchange, which is in a neighboring country and is an active market for the commodity that can rapidly absorb significant amounts of it. The F Exchange is the commodities exchange that is closest to Country W and is the primary exchange for the commodity in the broader geographical area. Entity B incurs transportation costs to deliver commodities to the F Exchange, and those costs typically result in a lower margin than when the commodities are sold in the active market in Country W. However, B sells the commodities on the F Exchange in certain instances, primarily when its transaction volume is seasonally abnormal or it is balancing its sales activities.

Typically, Country W would be considered the principal market for the commodity. However, identification of the principal market should be reassessed in each reporting period. If, in response to larger macroeconomic or other relevant factors, B were to temporarily cease transacting in Country W, the F Exchange could be viewed as the principal market.

Country W would generally be considered the principal market for the commodity on the basis of the following:

- There is a rebuttable presumption that, in the absence of evidence to the contrary, the market in which an entity normally would transact (i.e., the market in Country W) is the principal market.
- Country W has an active market that can rapidly absorb significant amounts of the commodity, and B has ready access to, as well as the ability to transact in, that market.
- Although the F Exchange constitutes an active market that B transacts in and has the ability to access, the F Exchange would not constitute B's principal market because:
  - Entity B normally transacts in the active market in Country W.
  - Transactions that B enters into on the F Exchange are executed primarily when B's transaction volumes are seasonally abnormal or it wants to balance its sales activities.
  - Given the transportation costs that it would incur to sell the commodity on the F Exchange, B concludes that the value is maximized when the sales occur on the active market in Country W.
  - Entity B typically has access to the market in Country W; from time to time, however, B may choose to sell the commodity on the F Exchange. Periodic ebb and flows of activity are not an indication that B must change the identification of its principal market.
Example 6-2 (continued)

If, however, there was a significant economic event, which caused a significant change in market conditions, including a lack of liquidity in the market in Country W, B may temporarily cease transacting in the market in Country W and may transact on the F Exchange. As a result, B may conclude that its principal market for the commodity has changed even if the change is temporary. However, in reaching such a conclusion, B should consider how long it expects to primarily transact on the F Exchange.

Example 6-3

Reassessment of Principal Market

Entity C buys and sells credit default swaps. The credit default swap market for some exposures is primarily a principal-to-principal or OTC market. The volume and level of activity for credit default swaps in the exchange market increase and decrease over time. In such cases, C may need to reassess the principal market and would not necessarily be limited by past volume or level of transactions in determining its principal market. In performing this assessment, C should consider the current activity level and expectations about how market participants will transact in the future as well as its ability to access the exchange market.

Example 6-4

Multiple Principal Markets in Consolidated Financial Statements

Parent D owns Subsidiary A, based in the United States, and Subsidiary B, based in Hong Kong. Both A and B own shares of XYZ, which is publicly traded on the NYSE and the Hong Kong Exchange (HKEx), and each market in shares of XYZ is considered active. Subsidiary A purchased its shares of XYZ on the NYSE, and B purchased its shares of XYZ on the HKEx. Both A and B are legally prohibited from transferring their investments in shares of XYZ to D or other subsidiaries of D. Both A and B recognize their XYZ shares at fair value through earnings. As of the end of the reporting period, A and B both measure the fair value of XYZ by using the price in the principal market, which they have determined to be their respective local stock exchanges because of differences in the ability to access the respective exchanges. ASC 820 specifies that if there is a principal market for the asset, the fair value measurement should represent the price in that market, even if the price in a different market is potentially more advantageous on the measurement date. Therefore, A would use the quoted price from the NYSE, which may be greater or less than the quoted price from the HKEx. Subsidiary B should use the quoted price from the HKEx, which may be greater or less than the quoted price from the NYSE.

If A and B were not legally prohibited from transferring their investments in shares of XYZ to D or related subsidiaries, both A and B would consider access to the HKEx and NYSE exchanges, respectively, through transfers. As a result, the reporting entity might have a single principal (or most advantageous) market for all subsidiaries (businesses) within the consolidated group that have invested in XYZ.
Chapter 7 — Market-Participant Assumptions

7.1 Characteristics of Market Participants

ASC 820-10

Market Participants

35-9 A reporting entity shall measure the fair value of an asset or a liability using the assumptions that market participants would use in pricing the asset or liability, assuming that market participants act in their economic best interest. In developing those assumptions, a reporting entity need not identify specific market participants. Rather, the reporting entity shall identify characteristics that distinguish market participants generally, considering factors specific to all of the following:

a. The asset or liability
b. The principal (or most advantageous) market for the asset or liability
c. Market participants with whom the reporting entity would enter into a transaction in that market.

The Fair Value Measurement Approach

55-1 The objective of a fair value measurement is to estimate the price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions. A fair value measurement requires a reporting entity to determine all of the following:

a. The particular asset or liability that is the subject of the measurement (consistent with its unit of account)
b. For a nonfinancial asset, the valuation premise that is appropriate for the measurement (consistent with its highest and best use)
c. The principal (or most advantageous) market for the asset or liability
d. The valuation technique(s) appropriate for the measurement, considering the availability of data with which to develop inputs that represent the assumptions that market participants would use when pricing the asset or liability and the level of the fair value hierarchy within which the inputs are categorized.
To meet the fair value measurement objective in ASC 820, an entity must develop assumptions that market participants would use to determine the price of an asset, liability, or equity instrument in an orderly transaction as of the measurement date. ASC 820 defines the term “market participants” as follows:

Buyers and sellers in the principal (or most advantageous) market for the asset or liability that have all of the following characteristics:

a. They are independent of each other, that is, they are not related parties, although the price in a related-party transaction may be used as an input to a fair value measurement if the reporting entity has evidence that the transaction was entered into at market terms [see Section 7.1.1].

b. They are knowledgeable, having a reasonable understanding about the asset or liability and the transaction using all available information, including information that might be obtained through due diligence efforts that are usual and customary [see Section 7.1.2].

c. They are able to enter into a transaction for the asset or liability [see Section 7.1.3].

d. They are willing to enter into a transaction for the asset or liability, that is, they are motivated but not forced or otherwise compelled to do so [see Section 7.1.4].

See Chapter 6 for discussion of the determination of the principal (or most advantageous) market.

7.1.1 Independence

As noted in the glossary definition above, market participants are considered independent when “they are not related parties.” However, the definition also indicates that “the price in a related-party transaction may be used as an input to a fair value measurement if the reporting entity has evidence that the transaction was entered into at market terms.” The determination that an exit price is at market terms can be considered comparable to the determination that a transaction between two parties was at arm’s length.

Paragraph BC25 of ASU 2011-04 discusses the requirement for market participants to be independent and states, in part:

Before the amendments, Topic 820 described market participants as being independent of the reporting entity. Because fair value assumes an orderly transaction between market participants at the measurement date and not an orderly transaction between the reporting entity and another market participant, the Board decided to clarify that the term independence in the definition of market participant means that market participants are independent of each other (that is, they are not related parties).

7.1.2 Knowledgeability

Market participants must be knowledgeable about the transaction. That is, they must have a “reasonable understanding about” the asset, liability, or equity instrument subject to the fair value measurement and, accordingly, need sufficient information to make a reasoned economic decision. In making such a decision, a market participant would perform the usual and customary due diligence that is part of an orderly transaction. An entity should use judgment in determining whether a potential buyer or seller is knowledgeable and has the necessary information to make a reasoned economic decision.

7.1.3 Ability to Enter Into a Transaction

Market participants must be capable of entering into a transaction for the asset, liability, or equity instrument subject to the fair value measurement. An entity must consider all relevant facts and circumstances in determining whether a potential buyer or seller is able to enter into a transaction, including the financial capabilities related to acquiring the asset, any potential legal restrictions, and any operational issues that would prevent the transaction from occurring.
7.1.4 Willingness to Enter Into a Transaction

Market participants must be “willing to enter into a transaction for” the asset, liability, or equity instrument subject to the fair value measurement (i.e., they must be “motivated but not forced or otherwise compelled to do so”). An entity must ensure that the potential buyer or seller is willing to enter into the transaction by considering all relevant facts and circumstances.

In a speech at the 2008 AICPA National Conference on Current SEC and PCAOB Developments, Muneera Carr, then a professional accounting fellow in the SEC's Office of the Chief Accountant, provided some of the SEC staff's views on the willingness of market participants to enter into a transaction. Ms. Carr stated, in part:

The [ASC 820] definition of fair value contemplates a hypothetical transaction that is both orderly and conducted between willing market participants. An orderly transaction is one where the asset or liability is marketed to potential buyers for a period that is usual and customary. In any environment but especially in the current one, transactions may result in pricing that potential sellers may not view as “favorable”. Unfavorable pricing or reduced liquidity do not constitute, in and of themselves, a distressed sale or a forced liquidation under [ASC 820] if the asset can be sold in a period that is usual and customary. Reduced transaction volume and wide bid-ask spreads may be helpful indicators in understanding whether market participants are willing to transact for the asset. However, judgment should be exercised to determine whether buyers and sellers in orderly transactions are those who are motivated but not forced to transact and therefore can be considered ‘willing market participants’. Said differently, while [ASC 820's] definition of fair value is based on an orderly transaction, it also states that such transactions should be between market participants and market participants are defined as both buyers and sellers willing to transact for an asset or liability because they are motivated rather than because they are forced to do so. [Footnotes omitted]

7.1.4.1 Unwillingness of a Seller to Transact at Current Prices

An entity’s unwillingness to transact at current prices for an asset it owns or a liability it owes is not a sufficient reason for such observable prices to be disregarded. ASC 820-10-35-54H states that “[a] reporting entity’s intention to hold the asset or to settle or otherwise fulfill the liability is not relevant when measuring fair value because fair value is a market-based measurement, not an entity-specific measurement.” However, an entity is responsible for determining fair value and must assess whether a price from an external source is representative of fair value as of the measurement date.

See Section 10.6.3.2 for further discussion of an entity’s unwillingness to transact at current prices.
7.2 Determining Market-Participant Assumptions

A fair value measurement is not entity-specific; rather, as indicated in ASC 820-10-35-9, an entity must “identify characteristics that distinguish market participants generally” by considering the asset, liability, or equity instrument subject to the fair value measurement; the principal (or most advantageous) market; and the “[m]arket participants with whom the reporting entity would enter into a transaction in that market.” This approach is consistent with the fair value objective (i.e., fair value is measured on the basis of assumptions used by market participants). An entity may not substitute its own assumptions for those of market participants.

In a speech at the 2009 AICPA National Conference on Current SEC and PCAOB Developments, Evan Sussholz, then a professional accounting fellow in the SEC’s Office of the Chief Accountant, discussed factors an entity should consider in determining market-participant assumptions and whether its own assumptions are comparable or different. Mr. Sussholz stated, in part:

*Question #3: Who are the potential market participants and what are their distinguishing characteristics?*

As you may know, Codification Topic 820 does not require a reporting entity to identify specific market participants. However, when measuring fair value it is important to understand the characteristics that distinguish market participants. The identification of these characteristics will play a significant role in understanding how market participants would use the asset being measured, along with the value that those market participants would place on that asset.

For example, let’s say there are two broad groups of market participants within the M&A market for a customer related intangible asset: financial buyers and strategic buyers. The strategic buyer group can be divided further into two categories: regional competitors and national competitors. In this example, the financial buyers, the regional competitors, and the national competitors would acquire this asset as a part of an M&A transaction for the entire entity and maximize value by operating this asset in conjunction with the other assets of the target business. However, the ultimate value that each group would place on the customer related intangible may depend on many factors including financial capacity, acquisition strategy, market participant synergies, market share, complementary assets, management capabilities, etc.

*Question #4: How do the market participant characteristics compare to the reporting entity's own characteristics?*

To answer this last question, a reporting entity should reconcile the significant distinguishing characteristics of the identified market participant groups to those of the reporting entity. The results of this reconciliation process will determine if the entity’s own assumptions should be adjusted to appropriately measure the fair value of an asset.

In our example, the reporting entity has determined the principal (or most advantageous) market, the highest and best use of the asset, along with the distinguishing characteristics of the potential market participants. For illustrative purposes, let’s say that the reporting entity has determined that a regional competitor would be the most likely market participant to acquire the customer related intangible asset and maximize value by operating this asset in conjunction with other assets. The reporting entity would then compare its own characteristics (both quantitative and qualitative factors) to those of a regional competitor to determine if its own assumptions are representative of market participant assumptions.

We anticipate that there may be instances when a reporting entity determines that its own assumptions are not significantly different than those of market participants. However, it is our expectation that a reporting entity will apply reasonable judgment when making this determination. The items that I just highlighted are just examples of the questions that I anticipate a reporting entity would consider in determining market participant assumptions. There are likely to be additional factors that one could consider when performing this analysis. Additionally, I would like to point out that the process of determining market participant assumptions can be iterative. Therefore, it is likely that questions will not always be answered sequentially, but will be answered continuously throughout the process of determining market participant assumptions.[1]

Lastly, I think it is reasonable to anticipate that the staff will continue to inquire about the process employed and judgments made by a reporting entity when developing market participant assumptions. Furthermore, we have observed that conversations are generally more productive when a reporting entity has documented how market participant assumptions were developed when performing a fair value measurement.
Example 7-1 further illustrates these concepts.

### Example 7-1

**Credit Risk of Receivables**

Entity A, a financial institution that has loan receivables from borrowers, is determining whether to include the borrower’s credit standing in the fair value measurement of the receivables. Because market participants would incorporate the borrower's credit standing into the valuation of a loan receivable, A must consider the borrower's credit standing in performing this measurement in accordance with ASC 820. The reason for this requirement is that the borrower's credit standing can potentially affect the proceeds that will be received from the borrower and market participants would take such considerations into account in determining the transaction price for these receivables.

### 7.3 Lack of Market Participants

In certain situations, there may be either a lack of market participants or limited information about the assumptions used by available market participants. Evan Sussholz, then a professional accounting fellow in the SEC’s Office of the Chief Accountant, addressed such situations in a speech at the 2009 AICPA National Conference on Current SEC and PCAOB Developments. Mr. Sussholz stated, in part:

> Now, I'd like to provide a few thoughts on developing market participant assumptions when measuring fair value.

> As many of you know, Codification Topic 820 requires that fair value measurements be performed from the perspective of market participants. While this requirement is easy to understand conceptually, the staff understands that some practitioners have encountered challenges trying to implement it in practice for assets and liabilities where observable pricing information is not available. In limited instances, market participant assumptions may not be readily available without undue cost and effort. Furthermore, it is possible that assumptions may vary substantially based on the facts and circumstances of each category of market participants. As a result, the lack of information or inability to obtain consistent information may present challenges in developing market participant assumptions when measuring fair value.

> Understanding these challenges, I wanted to provide you with our views of how one could look at developing market participant assumptions for fair value measurements. In general, I anticipate that most fair value measurements of assets or liabilities that trade in inactive markets or for which a market doesn’t exist will begin by looking at a reporting entity's own assumptions. These assumptions may include the reporting entity’s expected use of the asset, the asset’s life, and any related cash flow estimates from the use or sale of the asset. Using those assumptions as a starting point, reasonable judgment should be applied to determine if an entity's own assumptions are representative of market participant assumptions. We would suggest a reporting entity consider the following questions when performing this analysis. In order to illustrate how one might consider these questions in practice, I have also included a simplified example of a customer related intangible asset.
7.4 Multiple Market Participants With Different Assumptions

The following example from ASC 820-10-55-26 through 55-29 illustrates a situation in which there are multiple potential market participants and the entity is required to identify and consider the market-participant assumptions that maximize the fair value on the basis of the unit of valuation.

ASC 820-10

Case A: Asset Group

55-26 A reporting entity acquires assets and assumes liabilities in a business combination. One of the groups of assets acquired comprises Assets A, B, and C. Asset C is billing software integral to the business developed by the acquired entity for its own use in conjunction with Assets A and B (that is, the related assets). The reporting entity measures the fair value of each of the assets individually, consistent with the specified unit of account for the assets. The reporting entity determines that the highest and best use of the assets is their current use and that each asset would provide maximum value to market participants principally through its use in combination with other assets or with other assets and liabilities (that is, its complementary assets and the associated liabilities). There is no evidence to suggest that the current use of the assets is not their highest and best use.

55-27 In this situation, the reporting entity would sell the assets in the market in which it initially acquired the assets (that is, the entry and exit markets from the perspective of the reporting entity are the same). Market participant buyers with whom the reporting entity would enter into a transaction in that market have characteristics that are generally representative of both strategic buyers (such as competitors) and financial buyers (such as private equity or venture capital firms that do not have complementary investments) and include those buyers that initially bid for the assets. Although market participant buyers might be broadly classified as strategic or financial buyers, in many cases there will be differences among the market participant buyers within each of those groups, reflecting, for example, different uses for an asset and different operating strategies.

55-28 As discussed below, differences between the indicated fair values of the individual assets relate principally to the use of the assets by those market participants within different asset groups:

a. Strategic buyer asset group. The reporting entity determines that strategic buyers have related assets that would enhance the value of the group within which the assets would be used (that is, market participant synergies). Those assets include a substitute asset for Asset C (the billing software), which would be used for only a limited transition period and could not be sold on its own at the end of that period. Because strategic buyers have substitute assets, Asset C would not be used for its full remaining economic life. The indicated fair values of Assets A, B, and C within the strategic buyer asset group (reflecting the synergies resulting from the use of the assets within that group) are $360, $260, and $30, respectively. The indicated fair value of the assets as a group within the strategic buyer asset group is $650.

b. Financial buyer asset group. The reporting entity determines that financial buyers do not have related or substitute assets that would enhance the value of the group within which the assets would be used. Because financial buyers do not have substitute assets, Asset C (that is, the billing software) would be used for its full remaining economic life. The indicated fair values of Assets A, B, and C within the financial buyer asset group are $300, $200, and $100, respectively. The indicated fair value of the assets as a group within the financial buyer asset group is $600.

55-29 The fair values of Assets A, B, and C would be determined on the basis of the use of the assets as a group within the strategic buyer group ($360, $260, and $30). Although the use of the assets within the strategic buyer group does not maximize the fair value of each of the assets individually, it maximizes the fair value of the assets as a group ($650).
Chapter 8 — Fair Value Hierarchy

8.1 Introduction

8.1.1 General

ASC 820-10 — Glossary

**Level 1 Inputs**

Quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date.

**Level 2 Inputs**

Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

**Level 3 Inputs**

Unobservable inputs for the asset or liability.

The FASB established the fair value hierarchy in FASB Statement 157 (codified in ASC 820) to increase the consistency and comparability of fair value measurements and disclosures about such measurements. The hierarchy is divided into three categories on the basis of the relative observability and reliability of the inputs used in a fair value measurement. The categorization of inputs is important both to estimating fair value and to providing disclosures about such measurements.
With respect to measuring fair value, the fair value hierarchy focuses on inputs rather than valuation techniques. However, ASC 820-10-35-38 indicates that the availability of inputs and their relative subjectivity might affect the selection of the valuation technique. For example, a valuation technique in which an entity uses relevant inputs classified within Level 2 of the fair value hierarchy takes precedence over a valuation technique containing significant unobservable inputs (i.e., Level 3 inputs). In addition, with limited exceptions, an entity is precluded from using a valuation technique that employs Level 2 or Level 3 inputs if a Level 1 quoted market price in an active market is available for an asset, liability, or equity instrument subject to fair value measurement.

As discussed in Chapter 11, for recurring and nonrecurring fair value measurements, all entities are required to disclose the level of the fair value hierarchy within which the measurements are categorized in their entirety (i.e., Level 1, 2, or 3). Such disclosures are provided on the basis of the inputs used in the fair value measurements. As a result, it is critical that entities apply the guidance appropriately in assessing the appropriate level of the fair value hierarchy within which an item is measured or disclosed at fair value.

### 8.1.2 Determining the Classification of a Fair Value Measurement

**ASC 820-10**

**Fair Value Hierarchy**

**35-37A** In some cases, the inputs used to measure the fair value of an asset or a liability might be categorized within different levels of the fair value hierarchy. In those cases, the fair value measurement is categorized in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement. Assessing the significance of a particular input to the entire measurement requires judgment, taking into account factors specific to the asset or liability. Adjustments to arrive at measurements based on fair value, such as costs to sell when measuring fair value less costs to sell, shall not be taken into account when determining the level of the fair value hierarchy within which a fair value measurement is categorized.

**35-38A** If an observable input requires an adjustment using an unobservable input and that adjustment results in a significantly higher or lower fair value measurement, the resulting measurement would be categorized within Level 3 of the fair value hierarchy. For example, if a market participant would take into account the effect of a restriction on the sale of an asset when estimating the price for the asset, a reporting entity would adjust the quoted price to reflect the effect of that restriction. If that quoted price is a Level 2 input and the adjustment is an unobservable input that is significant to the entire measurement, the measurement would be categorized within Level 3 of the fair value hierarchy.

As noted in ASC 820-10-35-37A, inputs used in a fair value measurement “might be categorized within different levels of the fair value hierarchy.” As a result, the asset, liability, or equity instrument will be categorized in its entirety within a level of the fair value hierarchy on the basis of the lowest-level input that is significant to the fair value measurement.

To assess the level of the fair value hierarchy in which an asset, liability, or equity instrument should be categorized, an entity should first determine the inputs that it will use as part of its valuation technique for that instrument. The entity should then assess the level of the fair value hierarchy in which each input would be categorized in accordance with ASC 820-10-35-37 through 35-54A. See Sections 8.2, 8.3, and 8.4 for more information about Level 1, Level 2, and Level 3 inputs.

After assessing the level of the fair value hierarchy in which each input should be categorized, the entity should determine the lowest level of the fair value hierarchy in which an input that is significant to the fair value measurement is categorized. The entity should classify the entire asset, liability, or equity instrument in that level of the fair value hierarchy. For example, a fair value measurement that includes significant Level 2 inputs and significant Level 3 inputs would be classified in its entirety within Level 3.
ASC 820-10 does not establish a bright line for significance or mandate that significance be determined quantitatively. Rather, as noted in ASC 820-10-35-37A, an entity must use judgment in making this determination, “taking into account factors specific to the asset or liability.” Therefore, an entity should establish a method for determining whether an input is significant to a fair value measurement in its entirety and should apply this method consistently. The method might include a threshold or percentage of the overall measurement amount as a benchmark for significance. The threshold should represent a percentage of the overall measurement and not a percentage of a particular component of the measurement or the income statement effect of the measurement (i.e., the threshold should be based on a balance sheet approach). In determining significance for particularly complex valuations, an entity may need to consider how a particular input or inputs behave within a reasonable range of expected outcomes (i.e., a sensitivity analysis). Examples 8-1 through 8-3 illustrate how an entity might determine whether an unobservable input is significant to a fair value measurement.

**Example 8-1**

**Evaluation of Unobservable Volatility Input**

Entity A is evaluating whether the unobservable volatility input to a valuation technique used to measure the fair value of a hybrid financial instrument that contains an embedded option is significant to the overall fair value measurement. Entity A should consider the significance of the unobservable volatility relative to the hybrid financial instrument in its entirety and not solely the embedded option. Depending on the nature of the inputs to the hybrid financial instrument, A may need to perform a sensitivity analysis of the unobservable volatility input to determine its significance. Such an analysis might include considering how the unobservable volatility input affects the fair value of the hybrid financial instrument within a range of reasonable expected outcomes.

**Example 8-2**

**Evaluation of Adjustment Made to an Observable Transaction Price**

Recent transactions between independent third parties or between the entity and third parties (e.g., quoted prices in an inactive market, privately negotiated acquisitions, or dispositions of the entity's equity or debt) may be considered Level 2 inputs. This is the case if the transaction price meets the definition of fair value (i.e., the price represents an exit price for the item as of the date of the transaction, the transaction is not executed under duress, and the transaction is executed at terms that are consistent with how other market participants would transact).

In addition, an investor's recent acquisition or disposition of interests in the entity may be considered a Level 2 input if it meets the criteria above. For example, an investor may own a 25 percent equity investment in an entity that it recognizes at fair value. If the investor acquires another 10 percent equity investment in the entity and the acquisition meets the definition of fair value, the investor may use the price at which it acquired the additional 10 percent interest as a basis for valuing its entire 35 percent equity investment as of the next reporting date.

The investor must adjust the transaction price, if necessary, to appropriately measure the investment at fair value as of the reporting date. For example, the investor would adjust the transaction price for changes in the entity's financial position or for events that have occurred since the date of the transaction that would affect the fair value of the entity's shares. Unobservable adjustments that are significant to the measurement would render the fair value measurement of the investment a Level 3 measurement.
Example 8-3

Evaluation of Adjustment Made to a Level 2 Input

ASC 820-10-55-21(h) indicates that a “Level 2 input would be a valuation multiple (for example, a multiple of earnings or revenue or a similar performance measure) derived from observable market data, for example, multiples derived from prices in observed transactions involving comparable (that is, similar) businesses, taking into account operational, market, financial, and nonfinancial factors.” The market-derived multiple may be considered a Level 2 input; however, the historical financial measure (i.e., earnings or EBITDA) and any adjustments needed to reflect differences between the entity and comparable entities would most likely be Level 3 inputs because these factors are entity-specific and are not considered market-observable data. Therefore, the fair value measurement of the investment would most likely be classified within Level 3 of the fair value hierarchy.

Connecting the Dots

As discussed in Section 2.3.3, under ASC 810, a reporting entity that consolidates an eligible CFE may elect to measure the less observable of the fair value of the CFE’s financial assets or the fair value of the CFE’s financial liabilities by using the more observable of the two measurements (the “CFE fair value measurement alternative”). See ASC 810-10-15-17D for discussion of the eligibility requirements related to this fair value measurement alternative. In addition, ASC 810-10-30-10 through 30-16 and ASC 810-10-35-6 through 35-9 provide guidance on applying the CFE fair value measurement alternative to initial and subsequent fair value measurements, respectively.

When applying the CFE fair value measurement alternative, a reporting entity must disclose, for the financial assets and the financial liabilities of the CFE, the information required by ASC 820 on fair value measurement and by ASC 825 on financial instruments. Accordingly, the required disclosures apply to both the less observable and the more observable of the two measurements (although disclosures are not required for certain assets and liabilities that are incidental to the operations of the CFE and have carrying values that approximate fair value). In providing such disclosures, an entity must categorize the fair value measurement by level within the fair value hierarchy. ASC 810-10-50-21 states that for the less observable fair value measurement, the reporting entity must “disclose that the amount was measured on the basis of the more observable of the fair value of the financial liabilities and the fair value of the financial assets.”

To determine the level of the fair value hierarchy in which an entity should categorize the less observable fair value measurement, the reporting entity must first identify the inputs to the more observable fair value measurement. Such inputs include all of those used to calculate the fair value of the more observable measurement, which is described in the guidance in ASC 810-10-30-10 through 30-16 and ASC 810-10-35-6 through 35-9 on applying the CFE fair value measurement alternative.

For example, if the fair value of the CFE’s financial assets is more observable than the fair value of the CFE’s financial liabilities, the reporting entity should treat all of the following as inputs to the less observable fair value measurement (if applicable) in a manner consistent with ASC 810-10-30-12:

- The fair value of the financial assets, including (1) loans, (2) derivatives, and (3) the carrying values of any financial assets that are incidental to the CFE’s operations because the financial assets’ carrying values approximate their fair values.
- The carrying value of any nonfinancial assets held temporarily (e.g., real estate measured at historical cost less impairment).
• The fair value of any beneficial interests retained by the reporting entity (other than those that represent compensation for services).
• The reporting entity’s carrying value of any beneficial interests that represent compensation for services.

Next, the reporting entity must assess the observability of these inputs and determine whether the unobservable inputs are significant to the less observable fair value measurement. In performing this assessment, the entity must also consider any method used to allocate the amounts to the less observable fair value measurement, since such allocation is considered an input to the fair value measurement. The allocation may be performed on the basis of significant unobservable inputs, which would render the fair value measurement of the less observable measurement as a Level 3 measurement even if the fair value measurement of the more observable measurement is not categorized within Level 3.

The less observable fair value measurement cannot be categorized within Level 1 because the fair value measurement does not apply to the identical asset or liability.

8.2 Level 1 Inputs

8.2.1 General

ASC 820-10

*Level 1 Inputs*

35-40 Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date.

35-41 A quoted price in an active market provides the most reliable evidence of fair value and shall be used without adjustment to measure fair value whenever available, except as specified in paragraph 820-10-35-41C.

35-41C A reporting entity shall not make an adjustment to a Level 1 input except in the following circumstances:

a. When a reporting entity holds a large number of similar (but not identical) assets or liabilities (for example, debt securities) that are measured at fair value and a quoted price in an active market is available but not readily accessible for each of those assets or liabilities individually (that is, given the large number of similar assets or liabilities held by the reporting entity, it would be difficult to obtain pricing information for each individual asset or liability at the measurement date). In that case, as a practical expedient, a reporting entity may measure fair value using an alternative pricing method that does not rely exclusively on quoted prices (for example, matrix pricing). However, the use of an alternative pricing method results in a fair value measurement categorized within a lower level of the fair value hierarchy.

b. When a quoted price in an active market does not represent fair value at the measurement date. That might be the case if, for example, significant events (such as transactions in a principal-to-principal market, trades in a brokered market, or announcements) take place after the close of a market but before the measurement date. A reporting entity shall establish and consistently apply a policy for identifying those events that might affect fair value measurements. However, if the quoted price is adjusted for new information, the adjustment results in a fair value measurement categorized within a lower level of the fair value hierarchy.

c. When measuring the fair value of a liability or an instrument classified in a reporting entity’s shareholders’ equity using the quoted price for the identical item traded as an asset in an active market and that price needs to be adjusted for factors specific to the item or the asset (see paragraph 820-10-35-16D). If no adjustment to the quoted price of the asset is required, the result is a fair value measurement categorized within Level 1 of the fair value hierarchy. However, any adjustment to the quoted price of the asset results in a fair value measurement categorized within a lower level of the fair value hierarchy.
For a fair value measurement to qualify as a Level 1 measurement, or for an input into a fair value measurement to qualify as a Level 1 input, the price (input) must be a quoted price (unadjusted) in an active market for an identical asset or liability that the reporting entity can access as of the measurement date. Additional criteria for a Level 1 input are as follows:

- **Quoted price in an active market** — See Section 8.2.2 for more information about what constitutes an active market.

- **Unadjusted** — ASC 820-10-35-41C indicates that any adjustment (regardless of significance) to a fair value measurement (input) that would otherwise meet the Level 1 criteria results in a fair value measurement (input) that must be “categorized within a lower level of the fair value hierarchy.” See Section 8.2.3 for more information about adjustments to Level 1 inputs.

- **Identical asset or liability** — For a fair value measurement (input) to qualify as a Level 1 measurement (input), the price used in the fair value measurement must be for an identical asset or liability held by the reporting entity. See Examples 8-4 through 8-7 for more information.

- **Access to the price as of the measurement date** — The reporting entity must have access to the price as of the measurement date. For example, an entity has access to the price if it has the ability to transact at the price in an exchange market. An entity also has access if there are dealers that stand ready to transact with the entity at the price. Broker quotes alone are not sufficient evidence that the entity has access to the price if those brokers do not stand ready to transact at the price. Any adjustment made to a quoted price in an active market, because of limited or no market access, would result in a Level 2 or Level 3 measurement (input) depending on the nature of the adjustment. In addition, even if a quoted price in an active market is available, such pricing may not be readily accessible for each item being measured given the volume of instruments held by the reporting entity. As a result, a reporting entity may use alternative pricing (e.g., matrix pricing) as a practical expedient to measure fair value, but such a valuation would constitute a lower measurement within the fair value hierarchy. See Section 8.2.3 for more information.

Example 8-4 illustrates the fair value measurement of a debt security that is traded in a dealer market, which represents a Level 1 measurement.

**Example 8-4**

**Debt Security That Is Traded in a Dealer Market**

Entity A holds a debt security that is traded in a dealer market in which bid and ask prices are available. Assume that the market is active for the debt security, no adjustments have been made to the price, and the price is accessible by A.

If the price used to measure the fair value of the debt security is for the identical debt security held by A (i.e., the identical CUSIP), the debt security should be classified in Level 1 of the fair value hierarchy. The fact that the debt security is traded in a dealer market, as opposed to an exchange market, does not preclude the measurement of the debt security from being classified as a Level 1 measurement.

The ASC master glossary indicates that “[o]ver-the-counter markets (for which prices are publicly reported by the National Association of Securities Dealers Automated Quotations systems or by OTC Markets Group Inc.) [and] the market for U.S. Treasury securities” are dealer markets. Prices in dealer markets may be Level 1 measurements if all of the above criteria are met and the dealer market is active.
Example 8-5 illustrates the fair value measurement of an exchange-traded debt security, which represents a Level 1 measurement.

**Example 8-5**

**Exchange-Traded Debt Security Recognized as a Liability**

Entity B has issued an exchange-traded debt security and has elected to account for the liability for such issuance at fair value in accordance with the FVO. The identical instrument is currently trading as an asset in an active market. Entity B uses the quoted price for the asset as its initial input into the fair value measurement of its liability for the debt security. Entity B also evaluates whether the quoted price for the asset must be adjusted for factors such as third-party credit enhancements, which would not apply to the fair value measurement of the liability. Entity B determines that no adjustments need to be made to the quoted price of the asset.

Since the price used to measure the fair value of the debt security is for the identical debt security issued by B (i.e., the identical CUSIP) that actively is traded as an asset in an exchange market, and no adjustments to the quoted price of the instrument are required, the measurement of the debt security should be classified as a Level 1 measurement.

Example 8-6 illustrates an OTC forward contract that is classified as a Level 2 measurement because quoted prices in active markets are available only for similar securities.

**Example 8-6**

**OTC Forward Contract**

Entity C holds an OTC “look-alike” forward contract. The counterparty to this contract is contractually obligated to settle it on the basis of the quoted price for a similar futures contract traded on an active futures exchange. The forward contract meets the definition of a derivative and is therefore recorded at fair value.

While the look-alike forward contract mirrors — and its value is intended to approximate the quoted price for — the exchange-traded futures contract, the forward and futures contracts are not identical. Even if the counterparties to the forward contract both have the highest credit quality (resulting in the same level of credit risk as the exchange-traded futures contract), the forward contract is not considered identical because (1) the counterparties are different and (2) C cannot sell the forward contract on the futures exchange (i.e., the counterparty and liquidity risk related to the forward contract are greater than those related to the futures contract). While the measurement of a futures contract may be classified as a Level 1 measurement (in an active market), the measurement of the look-alike forward contract can only be classified as Level 2 or below.

Example 8-7 illustrates an interest rate swap for which observable inputs are used to determine fair value. Because the interest rate swap itself is not traded on an OTC market, the measurement of the swap cannot be classified as a Level 1 measurement.

**Example 8-7**

**OTC Interest Rate Swap**

Entity D is a party to an interest rate swap transacted on an OTC market. The OTC market does not quote prices for interest rate swaps. Entity D measures the fair value of the swap by using either (1) a discounted cash flow approach on the basis of observable market-based yield curves or (2) the price at which a similar swap was exchanged on the OTC market. While similar swaps may have been exchanged on the OTC market, these swaps would have different counterparties and would therefore not be identical to D’s swap.

The price at which D would be able to transfer the swap would result from a negotiated transaction in which the credit standings of the two parties to the swap, as well as the terms of the specific swap, are contemplated. Because the swap is not identical to the similar swap for which there are transactions on the OTC market, the fair value measurement of the swap would be classified as a Level 2 measurement (or a Level 3 measurement if any of the inputs that are significant to the measurement are unobservable inputs).
8.2.2 Active Markets

8.2.2.1 Active Versus Inactive Markets

**ASC 820-10 — Glossary**

**Active Market**
A market in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

**ASC 820-10**

**Measuring Fair Value When the Volume or Level of Activity for an Asset or a Liability Has Significantly Decreased**

35-54C The fair value of an asset or a liability might be affected when there has been a significant decrease in the volume or level of activity for that asset or liability in relation to normal market activity for the asset or liability (or similar assets or liabilities). To determine whether, on the basis of the evidence available, there has been a significant decrease in the volume or level of activity for the asset or liability, a reporting entity shall evaluate the significance and relevance of factors such as the following:

- There are few recent transactions.
- Price quotations are not developed using current information.
- Price quotations vary substantially either over time or among market makers (for example, some brokered markets).
- Indices that previously were highly correlated with the fair values of the asset or liability are demonstrably uncorrelated with recent indications of fair value for that asset or liability.
- There is a significant increase in implied liquidity risk premiums, yields, or performance indicators (such as delinquency rates or loss severities) for observed transactions or quoted prices when compared with the reporting entity’s estimate of expected cash flows, taking into account all available market data about credit and other nonperformance risk for the asset or liability.
- There is a wide bid-ask spread or significant increase in the bid-ask spread.
- There is a significant decline in the activity of, or there is an absence of, a market for new issues (that is, a primary market) for the asset or liability or similar assets or liabilities.
- Little information is publicly available (for example, for transactions that take place in a principal-to-principal market).

ASC 820-10-20 defines “active market,” and ASC 820-10-35-54C lists factors that may indicate that a market is not active because of a significant decrease in the volume or level of activity relative to normal market activity for the asset or liability (or similar assets or liabilities). In determining whether a market is active, an entity would focus on the trading activity of the individual asset or liability being measured rather than on the market in which it is traded. Therefore, a security that is traded infrequently on the NASDAQ could represent an asset that is not traded in an active market. In determining whether an active market exists for an asset or liability (or similar assets or liabilities), an entity should consider the factors discussed in ASC 820-10-35-54C only when the frequency and volume of the transactions for the asset or liability are not sufficient to provide ongoing relevant pricing information.

The presence of one or more of the factors in ASC 820-10-35-54C does not in itself mean that a market is not active. An entity should evaluate the relevance and significance of these factors to the individual asset, liability, or equity instrument measured at fair value to determine whether the market for the asset, liability, or equity instrument is not active. A market is not deemed inactive simply because of insufficient trading volume relative to the size of an entity’s position.
The characterization of a market as “active” or “inactive” may change as market conditions change. However, a decline in the volume of transactions for a particular asset or liability does not automatically make a market inactive. A market is considered active as long as the frequency and volume of transactions are sufficient to provide reliable ongoing pricing information.

**Connecting the Dots**

The level of market activity does not change the objective of a fair value measurement under ASC 820. ASC 820-10-35-54H states:

> Estimating the price at which market participants would be willing to enter into a transaction at the measurement date under current market conditions if there has been a significant decrease in the volume or level of activity for the asset or liability depends on the facts and circumstances at the measurement date and requires judgment. A reporting entity’s intention to hold the asset or to settle or otherwise fulfill the liability is not relevant when measuring fair value because fair value is a market-based measurement, not an entity-specific measurement.

A measurement that does not meet these objectives (e.g., a holder’s estimate of economic or fundamental value) is not a fair value measurement. An entity must consider market-participant assumptions when measuring fair value. If an entity determines that a market is inactive, it cannot use entity-specific assumptions instead of relevant observable market information in measuring fair value. See Section 10.6 for more information about measuring fair value when the volume or level of activity for an asset or liability has significantly decreased.

### 8.2.2.2 Multiple Active Markets

**ASC 820-10**

**Level 1 Inputs**

35-41B A Level 1 input will be available for many financial assets and financial liabilities, some of which might be exchanged in multiple active markets (for example, on different exchanges). Therefore, the emphasis within Level 1 is on determining both of the following:

a. The principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability

b. Whether the reporting entity can enter into a transaction for the asset or liability at the price in that market for the asset or liability at the measurement date.

35-46 Paragraph 820-10-55-42 illustrates the use of Level 1 inputs to measure the fair value of a financial asset that trades in multiple active markets with different prices.

An asset or liability may be exchanged in multiple active markets. For example, a security may be traded on several different exchanges. In these circumstances, fair value is measured on the basis of the entity’s principal market, or if a principal market does not exist, the most advantageous market for the asset or liability. An entity must be able to access a market as of the measurement date for this market to be the principal or most advantageous market.

Example 4 in ASC 820-10-55-42 through 55-45A illustrates how an entity would measure fair value for an asset that is sold in two different active markets. That example states that if one of the two markets is the entity’s principal market, that market must be used to measure the fair value of the asset. If neither market is considered the entity’s principal market, the fair value measurement is based on the most advantageous market. The example shows that the entity, in making this determination, must consider the transaction costs and transportation costs that would be incurred in each market. However, the fair value measurement in the most advantageous market is reduced only for transportation costs. See
Chapter 6 for more information about the determination of the principal or most advantageous market. See Sections 10.2.5.3 and 10.2.5.4 for discussion of transaction costs and transportation costs.

8.2.2.3 Active Market That Is Not a Secondary Market

A fair value measurement could be a Level 1 measurement even if there is no secondary market (e.g., an exchange market for the asset does not exist). This situation commonly applies to investments in registered open-ended mutual funds, which are illustrated in Example 8-8.

Example 8-8

Investment in Registered Open-Ended Mutual Fund

Entity E has an investment in an open-ended mutual fund, Fund B, that is registered under the Investment Company Act of 1940. Fund B is not listed on an exchange but publishes daily quotations of its NAV. Units are redeemed and purchased at the published NAV without any adjustment (i.e., Fund B's price is readily determinable since the published NAV is the basis for current transactions). There is no secondary market for the units because they are not transferable (i.e., the sole transactions are redemptions and purchases of the units by Fund B).

The fact that there is no secondary market for the units in Fund B (i.e., all transactions are between the fund and the unit holders) does not prevent E from classifying the fair value of its investment in Fund B within Level 1 of the fair value hierarchy if the conditions for Level 1 classification are met. In this example, E must evaluate whether the quoted price (i.e., the published NAV) is in an active market. For Fund B, pricing information is provided on an ongoing basis (and thus the active-market criteria are met), since the fund itself is a registered investment company, is obligated to stand ready to transact in either purchases or redemptions at the published NAV, and settles within seven days of investor redemption. In the absence of any evidence to the contrary (e.g., the fund is not able to settle an investor redemption in accordance with normal conventions because of underlying fund investment liquidity constraints), the investment in the registered open-ended investment company would meet the “active” criteria.

The assumption that the active-market criteria have been met is only related to determining the level of investments in open-ended mutual funds that are registered under the Investment Company Act of 1940.

It should also be noted that in this example, NAV is not being used as a practical expedient; rather, it represents fair value since the published NAV amounts reflect readily determinable fair values.

8.2.3 Adjustments to Level 1 Inputs

Generally, an entity should not adjust a Level 1 input in measuring the fair value of an asset or liability. However, ASC 820-10-35-41C notes the following three circumstances in which an adjustment may be made to a Level 1 input:

- A reporting entity holds a large number of similar (but not identical) assets or liabilities (e.g., debt securities) that are measured at fair value and, while a quoted price in an active market is available for each asset or liability, such quoted prices are not readily accessible for each of those assets or liabilities individually given the large number of similar assets or liabilities held by the entity as of the measurement date. Therefore, the entity uses an alternative pricing method such as matrix pricing.

- A quoted price in an active market does not represent fair value as of the measurement date because a significant event takes place after the close of a market but before the measurement date.

- The fair value measurement pertains to a liability or equity instrument, and the quoted price for the identical item traded as an asset in an active market must be adjusted for factors specific to the item or asset (see ASC 820-10-35-16D).
Further, the FASB stated the following in paragraph C68 of the Basis for Conclusions of Statement 157:

The Exposure Draft emphasized that a quoted price (unadjusted) in an active market should be used to measure fair value whenever it is available. Some respondents interpreted the related guidance as requiring the use of a quoted price in an active market without regard to whether that price is readily available or representative of fair value. Those respondents referred to possible conflicts with ASR 118, which requires adjustments to a quoted price in those situations (fair value pricing). In its redeliberations, the Board affirmed that its intent was not to preclude adjustments to a quoted price if that price is not readily available or representative of fair value, noting that in those situations, the market for the particular asset or liability might not be active. To convey its intent more clearly, the Board clarified that in those situations, the fair value of the asset or liability should be measured using the quoted price, as adjusted, but within a lower level of the fair value hierarchy.

In any of the above three situations, any adjustment to the quoted price renders the fair value measurement a Level 2 or Level 3 measurement.

8.2.4 Requirement to Use Level 1 Inputs

The size of a position held by an entity does not affect the categorization of the asset or liability within the fair value hierarchy, even if the normal daily trading or transaction volume would not be sufficient to absorb the entity's position. Fair value is not an entity-specific measurement; therefore, even if an entity expects to be unable to exit the position in a single transaction without adjusting the observable price, it would be inappropriate to use an input other than the quoted price in an active market. That is, a quoted market price (i.e., a Level 1 input) must be used to measure the fair value of an asset or liability that is traded in an active market on the basis of the product of the quoted price for the individual asset or liability and the quantity held by the entity.

8.3 Level 2 Inputs

8.3.1 General

Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
### ASC 820-10 (continued)

35-48 If the asset or liability has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset or liability. Level 2 inputs include the following:

- a. Quoted prices for similar assets or liabilities in active markets
- b. Quoted prices for identical or similar assets or liabilities in markets that are not active
- c. Inputs other than quoted prices that are observable for the asset or liability, for example:
  1. Interest rates and yield curves observable at commonly quoted intervals
  2. Implied volatilities
  3. Subparagraph superseded by Accounting Standards Update No. 2011-04
  4. Subparagraph superseded by Accounting Standards Update No. 2011-04
  5. Credit spreads.
  6. Subparagraph superseded by Accounting Standards Update No. 2011-04
- d. Market-corroborated inputs.

35-49 Paragraph 820-10-55-21 discusses Level 2 inputs for particular assets and liabilities.

#### Level 2 Inputs

55-21 Examples of Level 2 inputs for particular assets and liabilities include the following:

- a. Receive-fixed, pay-variable interest rate swap based on the London Interbank Offered Rate (LIBOR) swap rate. A Level 2 input would be the LIBOR swap rate if that rate is observable at commonly quoted intervals for substantially the full term of the swap.
- b. Receive-fixed, pay-variable interest rate swap based on a yield curve denominated in a foreign currency. A Level 2 input would be the swap rate based on a yield curve denominated in a foreign currency that is observable at commonly quoted intervals for substantially the full term of the swap. That would be the case if the term of the swap is 10 years and that rate is observable at commonly quoted intervals for 9 years, provided that any reasonable extrapolation of the yield curve for Year 10 would not be significant to the fair value measurement of the swap in its entirety.
- c. Receive-fixed, pay-variable interest rate swap based on a specific bank's prime rate. A Level 2 input would be the bank's prime rate derived through extrapolation if the extrapolated values are corroborated by observable market data, for example, by correlation with an interest rate that is observable over substantially the full term of the swap.
- d. Three-year option on exchange-traded shares. A Level 2 input would be the implied volatility for the shares derived through extrapolation to Year 3 if both of the following conditions exist:
  1. Prices for one-year and two-year options on the shares are observable.
  2. The extrapolated implied volatility of a three-year option is corroborated by observable market data for substantially the full term of the option.

In that case, the implied volatility could be derived by extrapolating from the implied volatility of the one-year and two-year options on the shares and corroborated by the implied volatility for three-year options on comparable entities' shares, provided that correlation with the one-year and two-year implied volatilities is established.

- e. Licensing arrangement. For a licensing arrangement that is acquired in a business combination and was recently negotiated with an unrelated party by the acquired entity (the party to the licensing arrangement), a Level 2 input would be the royalty rate in the contract with the unrelated party at inception of the arrangement.
f. Finished goods inventory at a retail outlet. For finished goods inventory that is acquired in a business combination, a Level 2 input would be either a price to customers in a retail market or a price to retailers in a wholesale market, adjusted for differences between the condition and location of the inventory item and the comparable (that is, similar) inventory items so that the fair value measurement reflects the price that would be received in a transaction to sell the inventory to another retailer that would complete the requisite selling efforts. Conceptually, the fair value measurement will be the same, whether adjustments are made to a retail price (downward) or to a wholesale price (upward). Generally, the price that requires the least amount of subjective adjustments should be used for the fair value measurement.

g. Building held and used. A Level 2 input would be the price per square foot for the building (a valuation multiple) derived from observable market data, for example, multiples derived from prices in observed transactions involving comparable (that is, similar) buildings in similar locations.

h. Reporting unit. A Level 2 input would be a valuation multiple (for example, a multiple of earnings or revenue or a similar performance measure) derived from observable market data, for example, multiples derived from prices in observed transactions involving comparable (that is, similar) businesses, taking into account operational, market, financial, and nonfinancial factors.

As noted in the guidance above, a Level 2 input represents an observable input that is not a Level 1 input. Level 2 inputs include:

- A quoted price for an identical asset or liability in an inactive market (see Section 8.2.2.1 for discussion of when a market is considered inactive).
- A quoted price for a similar asset or liability in an active or inactive market (see Section 8.3.1.1 below for discussion of the meaning of a similar asset or liability).
- Inputs other than quoted market prices that are observable for the asset or liability, such as interest rates, volatilities, and credit spreads.
- Market-corroborated inputs (see Section 8.3.1.2).

### 8.3.1.1 Similar Assets or Liabilities

In measuring the fair value of an asset, liability, or equity instrument for which a Level 1 measurement does not exist, an entity might use a quoted price for a “similar” asset or liability. As discussed in ASC 820-10-35-48, quoted prices for similar assets or liabilities represent Level 2 inputs. If an entity observes a quoted price in an inactive market for an identical asset or liability and determines that it is a relevant observable input for which no significant adjustment is required, typically little, if any, weight would be given to quoted prices for similar assets or liabilities. However, if a quoted price for the identical item being measured does not exist or must be adjusted (e.g., because the quoted price is not current), the entity may use quoted prices for similar assets or liabilities when applying a valuation technique to measure fair value.

An entity must use judgment in determining whether an asset or liability is “similar” to the asset or liability being measured at fair value. In making this determination, the entity must (1) understand the terms and other factors that affect the fair value of the asset or liability being measured and the asset or liability for which a quoted price exists and (2) identify and assess any differences in these terms and factors. Entities should also consider the extent to which adjustments to the quoted price may be necessary to reflect the effects of such differences. For example, entities may need to make adjustments to reflect differences in the condition, location, or risks (including nonperformance risk and liquidity risk) of the comparable items. Although a quoted price for a similar asset or liability is a Level 2 input, significant unobservable adjustments to that quoted price may render the fair value measurement a Level 3 measurement.
An entity may measure the fair value of a liability or equity instrument from the perspective of a market participant holding the item as an asset. In doing so, the entity might use the quoted price of an identical or similar liability or equity instrument that is traded as an asset. However, the quoted price should be adjusted for factors specific to the asset that do not apply to the fair value measurement of the entity's liability or equity instrument. ASC 820-10-35-16D(b) indicates, for example, that an adjustment may be required when “[t]he unit of account for the asset is not the same as for the liability or equity instrument. For example, for liabilities, in some cases the price for an asset reflects a combined price for a package comprising both the amounts due from the issuer and a third-party credit enhancement.” In addition, if the entity is measuring the fair value of a liability or equity instrument from the perspective of a market participant holding the identical item as an asset, and the asset held by another party includes a characteristic restricting its sale, in accordance with ASC 820-10-35-16D, “the fair value of the corresponding liability or equity instrument also would include the effect of the restriction.” However, if the liability or equity instrument is being measured on the basis of the quoted price of a similar asset, an adjustment to remove the effect of the restriction would generally be required if a quoted price for the identical asset, had it been available, would not have included a characteristic restricting its sale. Such adjustment may render the fair value measurement a Level 3 measurement.

**Connecting the Dots**

In October 2008, the IASB's Expert Advisory Panel issued a report, *Measuring and Disclosing the Fair Value of Financial Instruments in Markets That Are No Longer Active* (the “IASB Expert Advisory Panel report”), which describes practices entities use when measuring financial instruments at fair value. Paragraph 32 of the report gives the following examples of the basic terms of a financial instrument with contractual cash flows (entities may consider these terms, and any associated differences, when assessing whether the instrument being measured is “similar” to the instrument for which a quoted price exists):

(a) **the timing of the cash flows**: when the entity expects to realise the cash flows related to the instrument.

(b) **the calculation of the cash flows**: for example, for a debt instrument the interest rate that applies (i.e. the coupon), or for a derivative instrument how the cash flows are calculated in relation to the underlying instrument or index (or indices).

(c) **the timing and conditions for any options in the contract**: for example:

   (i) prepayment options (one or both parties can demand or make an early payment).

   (ii) extension options (one or both parties can extend the period of the instrument).

   (iii) conversion options (one or both parties can convert the instrument into another instrument).

   (iv) put or call options (one or both parties can exchange the instrument for a defined amount of cash or other assets or liabilities).

(d) **protection of the rights of the parties to the instrument**: for example:

   (i) terms relating to credit risk in debt instruments, such as collateral, event of default and margin call triggers.

   (ii) subordination of the instrument, for example the priority of the instruments in the event of a winding up.

   (iii) the legal enforceability of the cash flows.
Further, paragraph 33 of the report notes that “to measure the fair value of an instrument it is necessary to assess the return that market participants would require on the instrument to compensate for the risk related to:

(a) the amount and timing of the cash flows for the instrument.

(b) uncertainty about the ability of the counterparty to make payments when due (credit risk). This is a factor even if the counterparty is a financial institution.

(c) the liquidity of the instrument.”

This principle is consistent with the fair value measurement principles in ASC 820. Accordingly, in determining whether instruments are similar and whether an adjustment to a quoted price is necessary, an entity should consider any differences between (1) compensation that market participants would require for the risk associated with the instrument being measured and (2) compensation required for the instrument for which a quoted price exists. For example, the instrument being measured may be in greater relative supply than the instrument for which a quoted price exists. In this situation, a liquidity risk difference would need to be factored into the fair value calculation as an adjustment to the quoted price for the similar instrument.

See Section 10.1 for further discussion of the IASB Expert Advisory Panel report.

8.3.1.2 Market-Corroborated Inputs

ASC 820-10-35-48(d) indicates that Level 2 inputs can be market-corroborated inputs, which are defined as “[i]nputs that are derived principally from or corroborated by observable market data by correlation or other means.” It may be difficult to determine whether an input is correlated to observable market data. Correlation is a statistical concept indicating the strength and direction of a linear relationship between two variables. The same statistical thresholds (e.g., number of data points, 95 percent confidence level) applied in establishing that a hedging relationship under ASC 815 is highly effective under a regression analysis should be used in establishing correlation under ASC 820.

8.3.1.2.1 Inputs With Shorter Terms

An input used to measure the fair value of an asset or liability may only be observable for a portion of the life of the asset or liability. In these circumstances, the fair value measurement is a Level 2 measurement only if both of the following conditions are met:

- **Condition 1:** The input is observable for substantially the full term of the asset or liability — ASC 820-10-35-48 states, in part, “[i]f the asset or liability has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset or liability.” While not a bright line, if the input is observable for 90 percent or more of the term of the asset or liability, it would meet this condition.

- **Condition 2:** The impact of the unobservable period is not significant to the fair value of the asset or liability — When the input meets condition 1, the entity must consider ASC 820-10-55-21(b), which indicates that the effect of the unobservable term must not be significant to the measurement in its entirety for the measurement to be classified as Level 2. An entity must use judgment in determining whether the effect of the unobservable period is significant.
Example 8-9 illustrates how to consider market-corroborated inputs used in a fair value measurement.

### Example 8-9

**Power Purchase Agreement — Quoted Price for Substantially Full Term**

Entity E enters into a fixed-price four-year agreement to sell 50 MW of on-peak power for delivery at location ABC beginning on January 1, 20X2, and continuing through December 31, 20X5. On March 31, 20X2, E is determining the fair value of the agreement. Active market quotes are available for forward contracts to sell power at location ABC for three years (March 31, 20X2, to March 31, 20X5). Accordingly, E will use the three years of observable forward pricing data and develop an expectation for the remaining nine months (i.e., April 1 to December 31, 20X5) by employing a model that relies on pricing data and weather patterns from the previous four years. The model also incorporates all relevant physical constraints (e.g., capacity of existing and planned power plants near location ABC and projected supply and demand). The estimate for the remaining nine months represents an unobservable input.

Since the forward price curve is observable for only 36 of the 45 months (i.e., 80 percent of the term), it does not meet condition 1, which requires that the input be observable for substantially the full term. Therefore, the fair value measurement is a Level 3 measurement. Note that if the forward price curve had been observable for 90 percent or more of the term, E would still need to consider whether the effect of the unobservable term is significant to the fair value measurement to conclude that the measurement is a Level 2 measurement.

### 8.3.2 Adjustments to Level 2 Inputs

**ASC 820-10**

**Level 2 Inputs**

**35-50** Adjustments to Level 2 inputs will vary depending on factors specific to the asset or liability. Those factors include the following:

a. The condition or location of the asset

b. The extent to which inputs relate to items that are comparable to the asset or liability (including those factors described in paragraph 820-10-35-16D)

c. The volume or level of activity in the markets within which the inputs are observed.

**35-51** An adjustment to a Level 2 input that is significant to the entire measurement might result in a fair value measurement categorized within Level 3 of the fair value hierarchy if the adjustment uses significant unobservable inputs.

An entity may need to adjust Level 2 inputs to measure the fair value of an asset, liability, or equity instrument. Depending on the nature and significance of the adjustment, the fair value measurement of the entire asset, liability, or equity instrument may need to be categorized within Level 3 of the fair value hierarchy. See Section 8.4 for discussion of Level 3 inputs and Section 8.1.2 for discussion of how to categorize a fair value measurement containing multiple inputs that differ in terms of the categorization within the fair value hierarchy.
8.4 Level 3 Inputs

8.4.1 General

ASC 820-10

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<tr>
<th>Level 3 Inputs</th>
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<tr>
<td><strong>35-52</strong> Level 3 inputs are unobservable inputs for the asset or liability.</td>
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**35-53** Unobservable inputs shall be used to measure fair value to the extent that relevant observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. However, the fair value measurement objective remains the same, that is, an exit price at the measurement date from the perspective of a market participant that holds the asset or owes the liability. Therefore, unobservable inputs shall reflect the assumptions that market participants would use when pricing the asset or liability, including assumptions about risk.

**Level 3 Inputs**

**55-22** Examples of Level 3 inputs for particular assets and liabilities include the following:

a. Long-dated currency swap. A Level 3 input would be an interest rate in a specified currency that is not observable and cannot be corroborated by observable market data at commonly quoted intervals or otherwise for substantially the full term of the currency swap. The interest rates in a currency swap are the swap rates calculated from the respective countries' yield curves.

b. Three-year option on exchange-traded shares. A Level 3 input would be historical volatility, that is, the volatility for the shares derived from the shares' historical prices. Historical volatility typically does not represent current market participants' expectations about future volatility, even if it is the only information available to price an option.

c. Interest rate swap. A Level 3 input would be an adjustment to a mid-market consensus (nonbinding) price for the swap developed using data that are not directly observable and cannot otherwise be corroborated by observable market data.

d. Asset retirement obligation at initial recognition. A Level 3 input would be a current estimate using the reporting entity's own data about the future cash outflows to be paid to fulfill the obligation (including market participants' expectations about the costs of fulfilling the obligation and the compensation that a market participant would require for taking on the asset retirement obligation) if there is no reasonably available information that indicates that market participants would use different assumptions. That Level 3 input would be used in a present value technique together with other inputs, for example, a current risk-free interest rate or a credit-adjusted risk-free rate if the effect of the reporting entity's credit standing on the fair value of the liability is reflected in the discount rate rather than in the estimate of future cash outflows.

e. Reporting unit. A Level 3 input would be a financial forecast (for example, of cash flows or earnings) developed using the reporting entity's own data if there is no reasonably available information that indicates that market participants would use different assumptions.

Level 3 inputs are unobservable inputs used by an entity to measure the fair value of an asset, liability, or equity instrument. These inputs have the lowest level of priority under the fair value hierarchy and should only be used to the extent that observable inputs are not available. ASC 820-10-55-22 gives examples of Level 3 inputs. Example 8-10 illustrates the use of Level 3 inputs.
Example 8-10

Financial Forecast as Input Into a Fair Value Measurement

ASC 820-10-55-22(e) indicates that a “Level 3 input would be a financial forecast (for example, of cash flows or earnings) developed using the reporting entity's own data if there is no reasonably available information that indicates that market participants would use different assumptions.” While certain information an entity uses in applying a valuation technique may be observable (e.g., interest rate curves), the entity’s projected cash flows will most likely be significant to the fair value measurement. Therefore, the measurement would most likely be classified as Level 3.

8.4.2 Use of Best Data Available

8.4.2.1 General

ASC 820-10

Level 3 Inputs

A reporting entity shall develop unobservable inputs using the best information available in the circumstances, which might include the reporting entity's own data. In developing unobservable inputs, a reporting entity may begin with its own data, but it shall adjust those data if reasonably available information indicates that other market participants would use different data or there is something particular to the reporting entity that is not available to other market participants (for example, an entity-specific synergy). A reporting entity need not undertake exhaustive efforts to obtain information about market participant assumptions. However, a reporting entity shall take into account all information about market participant assumptions that is reasonably available. Unobservable inputs developed in the manner described above are considered market participant assumptions and meet the objective of a fair value measurement.

An entity must use the best available data in estimating unobservable inputs when a fair value measurement cannot be developed solely on the basis of observable inputs. The fair value hierarchy prioritizes inputs on the basis of their observability. Level 1 is the highest priority and Level 3 is the lowest priority. When an entity has concluded that a single valuation technique results in the most relevant information in terms of the fair value hierarchy (e.g., a Level 2 measurement vs. a Level 3 measurement), it should use that technique to calculate fair value. It would be inconsistent with the fair value hierarchy principles in ASC 820 for an entity to conclude that a Level 3 measurement is superior to a Level 2 measurement because relevant observable information about current market transactions is superior to entity-specific measurements.

For example, if management is able to use relevant observable market information to measure fair value under a market approach (a Level 2 measurement) and it uses significant unobservable information to measure fair value under an income approach (a Level 3 measurement), ASC 820 would require use of the Level 2 measurement even if the market is not active. However, in an inactive market, (1) there may be a lack of current observable market transactions for identical or similar assets or liabilities or (2) observable transactions may not be orderly. To produce a fair value measurement in such circumstances, an entity needs to perform further analysis and may have to adjust the market approach. If these adjustments are significant, they would render the fair value estimate under the market approach a Level 3 measurement. In such cases, entities may consider using multiple valuation techniques (e.g., a market approach and an income approach) to measure fair value.

When an entity considers multiple valuation techniques and determines that no one technique results in a superior fair value measurement under the fair value hierarchy, in accordance with ASC 820-10-35-24B, the entity is required to evaluate the results (or respective indications of fair value) of all techniques and weigh them, as appropriate. An entity may sometimes place more weight on one technique because it
uses more relevant observable inputs and therefore the fair value measurement determined under that technique is more indicative of fair value.

### 8.4.2.2 Use of Internal Information

An entity should not rely on internally developed assumptions or information if it has information indicating that market participants would use different assumptions or information in measuring the fair value of an asset, liability, or equity instrument. A fair value measurement is market-based but not entity-specific, as evident in the definition of fair value and discussed in a number of paragraphs in ASC 820, including the following:

- ASC 820-10-05-1C states that “[b]ecause fair value is a market-based measurement, it is measured using the assumptions that market participants would use when pricing the asset or liability, including assumptions about risk. As a result, a reporting entity’s intention to hold an asset or to settle or otherwise fulfill a liability [or instrument classified in a reporting entity’s shareholders’ equity] is not relevant when measuring fair value.”

- ASC 820-10-35-53 states that “[u]nobservable [Level 3] inputs shall be used to measure fair value to the extent that relevant observable [Level 1 and 2] inputs are not available.”

- ASC 820-10-35-54A states that “a reporting entity shall take into account all information about market participant assumptions that is reasonably available.”

- ASC 820-10-35-54E states that “[r]egardless of the valuation technique used [in measuring fair value], a reporting entity shall include appropriate risk adjustments, including a risk premium reflecting the amount that market participants would demand as compensation for the uncertainty inherent in the cash flows of an asset or a liability.”

For example, under an income approach, an entity generally uses a discounted cash flow technique to calculate the fair value of a financial asset and incorporates relevant observable inputs when available. Any unobservable inputs used in the fair value measurement, such as estimated future cash flows or risk adjustments incorporated into the discount rate, should be developed on the basis of management’s estimate of assumptions that market participants would use in pricing the asset in a current transaction as of the measurement date. If market data indicate that a significant liquidity discount applies in transactions involving comparable assets as of the measurement date, the entity should incorporate that information into its cash flow model (e.g., through an adjustment to the discount rate to compensate for the difficulty in selling the assets under current market conditions).

Example 8-11 illustrates when an entity’s own data should not be used because market-observable data are available.

### Example 8-11

Reliance on Internally Developed Assumptions When Market Assumptions Are Readily Available

Entity F is using a valuation model to measure the fair value of its holdings of privately placed corporate debt securities issued by Entity X. No quoted price for identical securities is available. Entity F’s valuation model uses assumptions about default rates and discount rates. Assumptions about default rates can be readily derived from current, relevant, observable market data for actively traded credit default swaps on X’s publicly traded bonds. To measure fair value, F cannot rely either on its own historical default data (for issuers with credit quality similar to X’s) or on its own default assumptions, even if the default assumptions are “stressed.” Instead, F should use the relevant market-observable assumptions about default rates.
8.4.3 Consideration of Risk in Inputs

In accordance with ASC 820-10-35-54, a fair value measurement should be adjusted for assumptions about risks that market participants would consider when valuing an asset, liability, or equity instrument. It may be difficult to determine what a market participant would demand as a risk adjustment in an assumed transaction, since such inputs may not be directly observable. In these situations, an entity should look beyond its own policies and transactions and consider the risks from a market participant’s perspective.

When using Level 3 inputs, an entity may need to consider the following items, when applicable, to incorporate market-participant assumptions:

- Recent transactions of a similar nature and duration.
- Common industry practices.
- Historical trends and settlements of past transactions.

See Section 10.4.2 for further discussion of the inclusion of risk adjustments in fair value measurements. See also Section 10.6 for further discussion of measuring fair value when the volume or level of activity for an asset or liability has significantly decreased.

8.5 Use of Pricing Services and Broker Quotes

8.5.1 General

Entities may use pricing service quotes or broker quotes to determine the fair value of certain assets, liabilities, or equity instruments. For example, mutual funds that carry large portfolios of investments at fair value and produce a daily NAV often obtain fair value information from third-party pricing service firms, brokers, or both.

The categorization in the fair value hierarchy of a broker quote or a quote obtained from a pricing service may be observable. However, without sufficient evidence, an entity cannot conclude that such quotes are observable and therefore represent Level 1 or Level 2 inputs. Likewise, an entity should not assume that such quotes are unobservable (i.e., Level 3 inputs). It is ultimately management’s responsibility to understand the fair value measurement techniques and inputs used so that it can (1) appropriately determine the level of the fair value hierarchy in which such fair value measurements are categorized and (2) conclude that the fair value measurements appropriately prioritize observable inputs.
8.5.2 Level 1 Inputs
Broker or pricing service quotes may only be considered Level 1 inputs if they represent the quoted price for an identical asset, liability, or equity instrument in an active market (see Sections 8.2.1 and 8.2.2).

8.5.3 Level 2 and Level 3 Inputs
Observable inputs are inputs that are developed by using market data and that reflect the assumptions market participants would use when pricing an asset, liability, or equity instrument. Level 2 inputs are inputs that are observable for the asset, liability, or equity instrument (other than Level 1 quoted prices), whereas Level 3 inputs are not observable.

If a quote from a pricing service or broker meets either of the following criteria, it is considered a Level 2 input:

- The entity can determine that market participants (i.e., a broker or others) have transacted, in an orderly transaction, for the asset or liability at the quoted price. For example, an entity might be able to corroborate the quoted price with the same or similar transactions that a broker or others have entered into. ASC 820-10-35-54I and 35-54J provide guidance on determining whether a transaction is or is not orderly when the market activity for an asset or liability has significantly declined (relative to normal market activity).\(^1\) If an entity is unable to determine whether a quoted price reflects a transaction that is or is not orderly, it must consider the quoted price in determining fair value, but the quoted price may not be the sole or primary basis for estimating fair value. In such cases, the quoted price needs to be significantly adjusted, potentially resulting in a Level 3 measurement.

- The entity can determine that the inputs the broker or pricing service used to arrive at the quoted price are observable and the Level 3 inputs used do not have a significant effect.

Depending on the item being measured at fair value, a quote from a broker or pricing service may represent one of many inputs or may be the only input into the fair value measurement. ASC 820-10-35-37A requires that “[i]n those cases, the fair value measurement [be] categorized in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.” See Section 8.1.2 for more information.

ASC 820-10-35-54D clarifies that a quoted price (e.g., a quote from a broker or pricing service) may not be determinative of fair value if the volume or level of market activity relative to normal market activity for the asset, liability, or equity instrument (or similar assets, liabilities, or equity instruments) has significantly declined. An entity should perform further analysis to determine whether it must significantly adjust the quoted price to measure fair value in accordance with ASC 820. For instance, if the only transactions underlying a quote are not orderly, the quote may not reflect fair value and little, if any, weight should be placed on it. In addition, a significant adjustment to the quoted price may be required if the price is not based on (1) current information that reflects orderly transactions or (2) a valuation technique that reflects market-participant assumptions (including assumptions about risks). Note that unobservable adjustments to a Level 2 input would render the entire measurement Level 3 if the adjustments are significant to the measurement in its entirety.

To determine whether a quote represents fair value, entities should also consider whether the quote is binding on the party making the quote or is available from more than one broker or pricing service. However, such facts do not necessarily indicate that the quote is “observable.” In other words, a binding quote does not necessarily meet one of the conditions described above. ASC 820-10-35-54M states

\(^1\) See Section 10.6 for more information.
that, when measuring fair value, an entity must take into account “the nature of a quote (for example, whether the quote is an indicative price or a binding offer) . . . when weighting the available evidence, with more weight given to quotes provided by third parties that represent binding offers.” See Section 10.8 for more information about the use of pricing services and broker quotes.

### 8.6 Certain Entities That Calculate NAV per Share (or Its Equivalent)

<table>
<thead>
<tr>
<th>ASC 820-10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)</strong></td>
</tr>
<tr>
<td><strong>35-54B</strong> An investment within the scope of paragraphs 820-10-15-4 through 15-5 for which fair value is measured using net asset value per share (or its equivalent, for example member units or an ownership interest in partners’ capital to which a proportionate share of net assets is attributed) as a practical expedient, as described in paragraph 820-10-35-59, shall not be categorized within the fair value hierarchy. In addition, the disclosure requirements in paragraph 820-10-50-2 do not apply to that investment. Disclosures required for an investment for which fair value is measured using net asset value per share (or its equivalent) as a practical expedient are described in paragraph 820-10-50-6A. Although the investment is not categorized within the fair value hierarchy, a reporting entity shall provide the amount measured using the net asset value per share (or its equivalent) practical expedient to permit reconciliation of the fair value of investments included in the fair value hierarchy to the line items presented in the statement of financial position in accordance with paragraph 820-10-50-2B.</td>
</tr>
</tbody>
</table>

As discussed in **Section 2.2.2**, ASC 820 provides a practical expedient for certain investments without a readily determinable fair value. An entity that elects this practical expedient should not categorize the asset within the fair value hierarchy when providing the disclosures required by ASC 820. See **Sections 10.9, 11.2.2.3, and 11.3.2.3** for further discussion of the use of this practical expedient.
Chapter 9 — Initial Measurement

9.1 Introduction

ASC 820-10

30-1 The fair value measurement framework, which applies at both initial and subsequent measurement if fair value is required or permitted by other Topics, is discussed primarily in Section 820-10-35. This Section sets out additional guidance specific to applying the framework at initial measurement.

30-2 When an asset is acquired or a liability is assumed in an exchange transaction for that asset or liability, the transaction price is the price paid to acquire the asset or received to assume the liability (an entry price). In contrast, the fair value of the asset or liability is the price that would be received to sell the asset or paid to transfer the liability (an exit price). Entities do not necessarily sell assets at the prices paid to acquire them. Similarly, entities do not necessarily transfer liabilities at the prices received to assume them.

30-3 In many cases, the transaction price will equal the fair value (for example, that might be the case when on the transaction date the transaction to buy an asset takes place in the market in which the asset would be sold). . . .

30-6 If another Topic requires or permits a reporting entity to measure an asset or a liability initially at fair value and the transaction price differs from fair value, the reporting entity shall recognize the resulting gain or loss in earnings unless that Topic specifies otherwise.

35-3 A fair value measurement assumes that the asset or liability is exchanged in an orderly transaction between market participants to sell the asset or transfer the liability at the measurement date under current market conditions.

As discussed in earlier chapters, fair value represents an exit price under the assumption that an asset is sold or a liability or equity instrument is transferred (assumed) in an orderly transaction between unrelated market participants under current market conditions. In many cases, the transaction price for an asset, liability, or equity instrument equals its fair value on initial recognition. However, in certain situations, it is not appropriate to assume that the transaction price (which is an entry price) is the initial fair value (which is an exit price) of an asset, liability, or equity instrument. That is, the entry price sometimes is not the exit price.

Paragraph C26 of the Basis for Conclusions of FASB Statement 157 states the following regarding the exit price notion that underlies a fair value measurement:

The transaction to sell the asset or transfer the liability is a hypothetical transaction at the measurement date, considered from the perspective of a market participant that holds the asset or owes the liability. Therefore, the objective of a fair value measurement is to determine the price that would be received for the asset or paid to transfer the liability at the measurement date, that is, an exit price. The Board concluded that an exit price objective is appropriate because it embodies current expectations about the future inflows associated with the asset and the future outflows associated with the liability from the perspective of market participants.
Note that the guidance in ASC 820 on initial fair value measurement only applies when other Codification topics require the initial recognition of an asset, liability, or equity instrument at fair value (see Table 2-1). However, because other Codification topics often do not require initial recognition at fair value, assets, liabilities, or equity instruments may be initially recognized at their transaction price even if that price differs from an exit price on initial recognition. Section 9.2 discusses the accounting in situations in which an asset, liability, or equity instrument must be initially recognized at fair value and the transaction price is not equal to the exit price on initial recognition. See Section 10.2.7 for further discussion of the application of ASC 820 to liabilities and instruments classified in an entity’s stockholders’ equity.

9.2 Transaction Price Is Not Fair Value

<table>
<thead>
<tr>
<th>ASC 820-10</th>
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<tbody>
<tr>
<td><strong>30-3A</strong> When determining whether fair value at initial recognition equals the transaction price, a reporting entity shall take into account factors specific to the transaction and to the asset or liability. For example, the transaction price might not represent the fair value of an asset or a liability at initial recognition if any of the following conditions exist:</td>
</tr>
<tr>
<td>a. The transaction is between related parties, although the price in a related party transaction may be used as an input into a fair value measurement if the reporting entity has evidence that the transaction was entered into at market terms.</td>
</tr>
<tr>
<td>b. The transaction takes place under duress or the seller is forced to accept the price in the transaction. For example, that might be the case if the seller is experiencing financial difficulty.</td>
</tr>
<tr>
<td>c. The unit of account represented by the transaction price is different from the unit of account for the asset or liability measured at fair value. For example, that might be the case if the asset or liability measured at fair value is only one of the elements in the transaction (for example, in a business combination), the transaction includes unstated rights and privileges that are measured separately, in accordance with another Topic, or the transaction price includes transaction costs.</td>
</tr>
<tr>
<td>d. The market in which the transaction takes place is different from the principal market (or most advantageous market). For example, those markets might be different if the reporting entity is a dealer that enters into transactions with customers in the retail market, but the principal (or most advantageous) market for the exit transaction is with other dealers in the dealer market.</td>
</tr>
</tbody>
</table>

| **30-5** Paragraph 820-10-55-46 illustrates situations in which the price in a transaction involving a derivative instrument might (and might not) equal the fair value of the instrument. |
As discussed above, transaction prices often will equal fair value on initial recognition. However, if a transaction is carried out under duress or is between related parties, or if other factors are present, the transaction price may not equal fair value on initial recognition. Therefore, an entity needs to take additional considerations into account in determining the fair value on initial recognition of an asset, liability, or equity instrument.

Table 9-1 gives examples of factors that may suggest that the transaction price does not represent the fair value of an asset, liability, or equity instrument on initial recognition.

Table 9-1

<table>
<thead>
<tr>
<th>Factor</th>
<th>Example(s)</th>
</tr>
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<tbody>
<tr>
<td>The transaction is between related parties, although the price in a</td>
<td>A parent company purchases a portfolio of troubled loans from its wholly owned subsidiary. The price exceeds the fair value because it incorporates a capital contribution from the parent to the subsidiary. ASC 850 contains guidance on determining whether a transaction is a related-party transaction.</td>
</tr>
<tr>
<td>related-party transaction may be used as an input into a fair value</td>
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<tr>
<td>measurement if the entity has evidence that the transaction was</td>
<td></td>
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<tr>
<td>entered into at market terms.</td>
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<tr>
<td>The transaction takes place under duress or the seller is forced to</td>
<td>A hedge fund divests itself of nonmarketable assets to stave off a liquidity crisis. Thus, there was not adequate exposure to the market before the measurement date to allow for usual and customary marketing activities for transactions involving such assets or liabilities.</td>
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<tr>
<td>accept the price in the transaction because of urgency (e.g., the</td>
<td></td>
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<tr>
<td>seller is experiencing financial difficulty).</td>
<td></td>
</tr>
<tr>
<td>The unit of account represented by the transaction price differs from</td>
<td>A multiple-element transaction in which the asset or liability measured at fair value is only one of the elements in the transaction (e.g., in a business combination).</td>
</tr>
<tr>
<td>the unit of account for the asset or liability measured at fair value.</td>
<td></td>
</tr>
<tr>
<td>A transaction includes unstated rights and privileges that should be</td>
<td>A debt instrument is issued with an inseparable third-party credit enhancement (see Section 4.3.2.2).</td>
</tr>
<tr>
<td>separately measured (e.g., the seller of real estate grants a non-</td>
<td>The transaction price includes transaction costs. See Section 10.2.5.3 for further discussion of transaction costs.</td>
</tr>
<tr>
<td>interest-bearing loan to the buyer).</td>
<td></td>
</tr>
<tr>
<td>The market in which the transaction takes place differs from the</td>
<td>The transaction price of the interest rate swap (e.g., zero) does not necessarily represent fair value from the dealer’s perspective at initial recognition. The dealer has access to the dealer market (i.e., with dealer counterparties).</td>
</tr>
<tr>
<td>principal or most advantageous market.</td>
<td></td>
</tr>
</tbody>
</table>

1 In the absence of such factors, the initial fair value of an asset, liability, or equity instrument would be its transaction price.
ASC 820-10-55-46 through 55-49 also include the following example illustrating a situation in which it would not be appropriate to presume that the transaction price represents fair value as of the date of initial recognition.

**Example 5: Transaction Prices and Fair Value at Initial Recognition — Interest Rate Swap at Initial Recognition**

55-46 This Topic (see paragraphs 820-10-30-3 through 30-3A) clarifies that in many cases the transaction price, that is, the price paid (received) for a particular asset (liability), will represent the fair value of that asset (liability) at initial recognition, but not presumptively. This Example illustrates when the price in a transaction involving a derivative instrument might (and might not) equal the fair value of the instrument at initial recognition.

55-47 Entity A (a retail counterparty) enters into an interest rate swap in a retail market with Entity B (a dealer) for no initial consideration (that is, the transaction price is zero). Entity A can access only the retail market. Entity B can access both the retail market (that is, with retail counterparties) and the dealer market (that is, with dealer counterparties).

55-48 From the perspective of Entity A, the retail market in which it initially entered into the swap is the principal market for the swap. If Entity A were to transfer its rights and obligations under the swap, it would do so with a dealer counterparty in that retail market. In that case, the transaction price (zero) would represent the fair value of the swap to Entity A at initial recognition, that is, the price that Entity A would receive to sell or pay to transfer the swap in a transaction with a dealer counterparty in the retail market (that is, an exit price). That price would not be adjusted for any incremental (transaction) costs that would be charged by that dealer counterparty.

55-49 From the perspective of Entity B, the dealer market (not the retail market) is the principal market for the swap. If Entity B were to transfer its rights and obligations under the swap, it would do so with a dealer in that market. Because the market in which Entity B initially entered into the swap is different from the principal market for the swap, the transaction price (zero) would not necessarily represent the fair value of the swap to Entity B at initial recognition.

An initial difference between the transaction price and fair value may also result from an entity’s election to use mid-market pricing or other pricing conventions as a practical expedient in accordance with ASC 820-10-35-36D. See Example 9-2 for an illustration of this concept.

**Connecting the Dots**

ASC 946 requires investment companies to report investments (including investments in securities, common stock, or partnership interests for which market quotations are not readily available, such as private equity investments) at fair value as of each reporting date. An entity may also measure equity investments at fair value through earnings under ASC 321.

At initial recognition, an entity may be able to conclude that the initial transaction price (excluding transaction costs) is fair value (or may conclude that the equity security should be initially recognized at the transaction price). For subsequent reporting periods, ASC 820 requires entities to (1) use an appropriate valuation technique or combination of techniques to measure fair value (see ASC 820-10-35-24B) and (2) apply the valuation technique(s) consistently unless a change results in a measurement that is equally or more representative of fair value (see ASC 820-10-35-25). For private equity investments, valuation techniques that may be appropriate include market approaches (such as multiples of earnings) and income approaches (such as free cash flows-to-equity discount). While an entity may use the initial transaction price (excluding transaction costs) as a starting point for valuations on subsequent reporting dates (e.g., by calibrating certain parameters of its valuation model), it cannot assume that the initial
transaction price (excluding transaction costs) equals fair value for subsequent reporting periods.

In applying valuation techniques, an entity should consider whether any change has occurred in factors affecting the investment's fair value and should update its fair value measurement accordingly. Such considerations include market conditions (such as equity market conditions, discount rates, or market risk premiums) and investment-specific factors (such as projected cash flows or entity-specific risk factors). The following nonexhaustive list of factors for entities to consider in estimating the fair value of securities for which market quotations are not available is based, in part, on ASC 940-820-30-1:

- The issuer's financial standing.
- The issuer's business and financial plan.
- The cost as of the purchase date.
- The liquidity of the market.
- Contractual restrictions on salability.
- Pending public offerings for the financial instrument.
- Pending reorganization activity affecting the financial instrument (such as merger proposals, tender offers, debt restructurings, and conversions).
- Reported prices and the extent of public trading in similar financial instruments of the issuer or comparable entities.
- The issuer's ability to obtain needed financing.
- Changes in the economic conditions affecting the issuer.
- A recent purchase or sale of the entity's security.
- Pricing by other dealers in similar securities.

### 9.2.1 Inception Gains and Losses

If fair value is the initial measurement attribute under other Codification topics, an entity needs to assess whether the transaction price represents fair value at inception by considering factors specific to the transaction, including whether one or more of the factors in ASC 820-10-30-3A are present. In many cases, it is inappropriate to record an inception gain or loss as of the date of initial recognition of an asset or liability.

At the 2006 AICPA National Conference on Current SEC and PCAOB Developments, Joseph D. McGrath, a professional accounting fellow in the SEC’s Office of the Chief Accountant, stated the following:

> Given [ASC 820’s] exit price notion, fair value at initial recognition is [not] limited to transaction price. Rather, [ASC 820] states that the entity “shall consider factors specific to the transaction and the asset or liability.” [Footnote omitted] One such factor is whether the transaction occurs in a market other than the entity’s principal market. [Example 5 in ASC 820-10-55-46 through 55-49] illustrates this concept with the example of a securities dealer transacting with a customer in the retail market. In this example, the dealer’s fair value is not necessarily transaction price, since its principal market to exit the transaction may be different. . . .

> We have heard that some believe that it is “open season” on inception gains. I would caution those constituents that there continue to be many instances in which day one gains are not appropriate. [ASC 820] does not allow the practice of “marking to model” when the transaction occurs in the entity’s principal market. Rather, transaction prices would generally be used in such a circumstance, and the model would be calibrated to match transaction price. Continuing with the previous example, if the securities dealer transacts with another in the dealer market, absent satisfaction of any of the criteria in [ASC 820-10-30-3A], transaction price would likely be the best estimate of the fair value. As a result, there would not be any inception gain.
Some have asserted that the use of a pricing model would automatically lead to day two gains even in situations where there was not an inception gain. Again, a word of caution, assuming that an entity uses a pricing model to value its transaction in subsequent periods, [ASC 820] would indicate that the pricing model should be calibrated, so that the model value at initial recognition equals transaction price. As a result of calibrating the model, simply using a pricing model to determine fair value would not result in day two gains, unless there were changes in the underlying market conditions. [Footnote omitted]

Mr. McGrath’s remarks indicate that if none of the factors in ASC 820-10-30-3A are present, the transaction price is most likely the best estimate of fair value. However, if any of the criteria in ASC 820-10-30-3A are met, there may be a difference between the transaction price and fair value. For example, ASC 820-10-30-3A(c) indicates that the transaction price might not represent fair value at initial recognition if “the transaction price includes transaction costs.” That might be the case in a transaction that includes a structuring fee. In such a situation, entities should consider adjusting a model value for the profit margin that another market participant would demand in a transaction to transfer the instrument. This is consistent with the risk adjustment discussion in the ASC 820-10-20 definition of inputs.

The following examples illustrate the concepts discussed above related to the recognition of inception gains and losses.

**Example 9-1**

**Interest Rate Swap Entered Into Between Retail Counterparty and Dealer**

A retail counterparty enters into an interest rate swap with a dealer for no initial consideration (i.e., the transaction price is zero). Assume that the valuation model used to determine the fair value of the interest rate swap at inception is significantly influenced by unobservable inputs. The initial model value is a $1 million loss. The retail counterparty should not conclude that the transaction price represents fair value on initial recognition without further consideration. Instead, the retail counterparty needs to assess whether the transaction price represents fair value by considering factors specific to the transaction, including whether one or more of the following factors in ASC 820-10-30-3A are present:

- The retail counterparty and the dealer are related parties.
- The retail counterparty enters into the transaction under duress or is otherwise forced to accept the price in the transaction.
- The transaction price is related to a unit of account that includes elements other than the asset or liability measured at fair value, such as an unstated right or privilege, another element, or transaction costs. For example, a retail counterparty may agree to a price that includes an embedded structuring fee (i.e., a transaction cost) for services that have already been rendered by a dealer. In this case, the retail counterparty would separately account for the structuring fee in accordance with another Codification topic. Depending on the nature of the structuring fee, the retail counterparty may recognize a separate expense (i.e., a loss) at inception.
- The retail counterparty’s transaction does not occur in the principal or most advantageous market.

Notwithstanding the preceding discussion, inception gains for retail counterparties that are due to factors specific to the financial instrument with significant unobservable inputs are expected to be infrequent, and all entities should clearly document their ASC 820-10-30-3A analysis and assertions. Inception losses, however, are more common for retail counterparties as a result of bid-ask spread differences between the entry transaction and the hypothetical exit transaction. This is illustrated in **Example 9-2**.
Chapter 9 — Initial Measurement

Example 9-2

Debt Security Purchased by Nondealer

Assume the following:

- A nondealer purchases a debt security from a dealer at the ask price of $101.
- The current market-observable bid price is $99.
- The nondealer’s policy is to use a mid-level price ($100) for its fair value measurements.

By paying $101 (the ask price) and then immediately measuring the fair value at the mid-level price of $100, the nondealer will have incurred an inception loss of $1. This example illustrates how a nondealer might incur a loss at inception because of its policy for determining fair value within the bid-ask spread. That is, a nondealer may incur an inception loss depending on (1) where it has initially transacted within or outside the bid-ask spread and (2) its bid-ask pricing policy. An entity should apply the guidance in ASC 820-10-35-36C and 35-36D to determine its bid-ask pricing policy.

In some cases, an entity is prohibited from recognizing an inception gain or loss even if the transaction price is not fair value at inception of the contract. For example, ASC 815-15-30-2 provides guidance on determining the initial carrying amount of a host contract and an embedded derivative when separate accounting is required by ASC 815-15. ASC 815-15-30-2 requires that an entity use the “with-and-without” method to calculate the initial carrying amount of the host contract. Under the with-and-without method, the initial carrying amount of the embedded derivative component of a hybrid instrument is equal to its fair value at inception of the contract (as determined under ASC 820), and the initial carrying amount of the host contract equals the excess of the transaction price for the hybrid instrument over the initial fair value of the embedded derivative.

In a speech at the 2003 AICPA National Conference on Current SEC Developments, John James, then a fellow in the SEC’s Office of the Chief Accountant, clarified that when using the with-and-without method, an entity is not permitted to recognize an “immediate gain or loss that would occur if the relative fair value method were used” (the relative fair value method is not permitted). Mr. James discussed a situation in which the SEC staff objected to an entity’s recognition of a day 1 gain on an embedded derivative when the entity believed that if that embedded derivative were issued on a freestanding basis, the entity would have met the conditions to recognize such a gain. The staff believed that ASC 815 was prescriptive regarding the initial measurement for both the host contract and bifurcated derivative (i.e., the with-and-without method).

On the basis of this speech, it would not be appropriate for an entity to record an inception gain or loss for a hybrid instrument with an embedded derivative that must be bifurcated and accounted for separately in accordance with ASC 815-15. Rather, the difference between the basis of the hybrid instrument and the inception-date fair value of the embedded derivative should be recorded as the initial carrying amount of the host contract. As a result, any day 1 gains and losses (observable or unobservable) related to separately measured embedded derivatives effectively would be applied to the basis of the host contract and recognized as the host contract affects earnings (e.g., amortized as a yield adjustment to a nonderivative host financial instrument). For hybrid instruments not carried at fair value in their entirety, entities should apply the guidance from ASC 815-15-30-2 and the related SEC speech. These requirements do not apply to hybrid instruments recognized at fair value in their entirety.
9.3 Model Calibration

ASC 820-10

Valuation Techniques

35-24C If the transaction price is fair value at initial recognition and a valuation technique that uses unobservable inputs will be used to measure fair value in subsequent periods, the valuation technique shall be calibrated so that at initial recognition the result of the valuation technique equals the transaction price. Calibration ensures that the valuation technique reflects current market conditions, and it helps a reporting entity to determine whether an adjustment to the valuation technique is necessary (for example, there might be a characteristic of the asset or liability that is not captured by the valuation technique). After initial recognition, when measuring fair value using a valuation technique or techniques that use unobservable inputs, a reporting entity shall ensure that those valuation techniques reflect observable market data (for example, the price for a similar asset or liability) at the measurement date.

When an entity determines that a transaction price represents fair value on initial recognition, but the valuation model that the entity expects to use for subsequent measurement yields an initial estimate of fair value that differs from the transaction price, the valuation model should be calibrated in such a way that it yields the same estimate of fair value as the transaction price. An entity should not recognize a gain or loss at inception because of a difference between the valuation model and the transaction price. An inception gain or loss would only be recognized as a result of subsequent changes in circumstances.

ASC 820-10-35-24C does not specify how to calibrate a model or model inputs. Accordingly, various calibration methods may be acceptable under ASC 820-10-35-24C depending on the valuation technique used, the availability of information about market-participant assumptions (e.g., relevant observable inputs), the terms of the instrument, and the nature of the entity’s portfolio. However, regardless of the method an entity uses, if the transaction price represents the fair value of a contract at inception and the initial fair value differs from the entity’s inception-date model value, the inception difference should not be recognized (1) upon the initial recognition of the transaction or (2) after initial recognition unless there has been a subsequent change in circumstances. Instead, the inception difference should be recognized as the uncertainty in the inputs, the uncertainty in the model, or both are eliminated. The calibration method chosen should be applied systematically, rationally, and consistently.

As noted above, the appropriate method for calibrating a model depends on an entity’s circumstances. Entities often employ valuation adjustments to reflect the factors that market participants would consider in setting a price when those factors are not otherwise captured in the model (e.g., adjustments for uncertainty in model inputs or model complexity). Appropriate use of valuation adjustments should result in an estimate of fair value that reflects the price at which market participants would transact as of the reporting date. Similarly, to comply, at initial recognition, with the fair value measurement objective prescribed by ASC 820-10-30-3A and ASC 820-10-35-24C, an entity may determine that it needs to make a separate valuation adjustment to calibrate its model (and to ensure that the inception difference is not recognized). In these situations, the entity should review the valuation adjustment periodically to ensure that it reflects any new information and is consistent with ASC 820’s exit price notion. ASC 820-10-35-24C indicates that “[a]fter initial recognition, when measuring fair value using a valuation technique or techniques that use unobservable inputs, a reporting entity shall ensure that those valuation techniques reflect observable market data (for example, the price for a similar asset or liability) at the measurement date.”
Example 9-3 illustrates a model calibration approach that may be acceptable when the inception difference can be isolated to a particular unobservable input. Entities should follow the steps in the example below regardless of whether the calibration approach results in direct adjustments to model inputs or valuation adjustments to the modeled estimate of fair value.

Example 9-3

Model Calibration for Electricity Contract

Entity A enters into an electricity forward contract to purchase 100 MW of electricity (daily) at Location X for a 10-year term. The forward contract is accounted for at fair value because it meets the definition of a derivative and does not qualify for (or the entity did not elect) the scope exception for normal purchases and normal sales under ASC 815-10-15-22 through 15-26. There are three years of observable forward prices at Location X. Entity A's model value at inception is a gain of $1 million; however, no cash was exchanged between the parties. On the basis of an analysis under ASC 820-10-30-3A, A determines that the transaction price equals the exit price (i.e., fair value equals zero at inception) and that it must apply ASC 820-10-35-24C. The only unobservable input with a significant effect on the model value at inception is the forward electricity price for Location X.

In this scenario, A might apply ASC 820's calibration guidance as follows:

• **Step 1: Identify the source of the inception difference** — Entity A has established that the only unobservable input that significantly affects the model value is forward electricity prices.

• **Step 2: Adjust the unobservable inputs or establish valuation adjustments in such a way that the adjusted model value equals the transaction price at inception** — In a systematic, rational, and consistently applied manner, adjust the unobservable forward price points (i.e., years 4–10) on the forward price curve in such a way that the model produces a fair value equal to zero (i.e., the exit price equals the transaction price).

When calibration results in direct adjustment to model inputs, entities should consider the impact of such adjustments on the valuation of other instruments in their portfolio (e.g., instruments valued under different models but by using the same or similar pricing inputs). The calibration may affect the valuation of other instruments because the calibrated inputs may replace or supersede the assumptions previously used for unobservable inputs. Recall that in step 1, A determined that the inception difference was driven solely by the unobservable Location X electricity prices; therefore, any resulting "calibration adjustment" represents a calibration of these unobservable electricity prices to the most recent available information (the forward contract's transaction price). As a result, if A derives the fair value of a portfolio of contracts by using long-dated (in this example, beyond three years) Location X electricity prices, the calibration adjustment to the electricity forward prices would most likely affect the fair value of the other long-dated Location X contracts. The considerations noted above for calibration techniques that result in direct adjustment to model inputs may also apply when a calibration results in valuation adjustments to the modeled estimate of fair value. In other words, calibration adjustments result in updated information about assumptions market participants use in assessing unobservable inputs or valuation adjustments and may have relevance beyond the recently executed transaction.

• **Step 3: Recognize subsequent changes in model value** — The inception difference will be recognized when (1) unobservable inputs become observable or (2) unobservable inputs or valuation adjustments are adjusted to reflect new information (e.g., through calibration of the model or model inputs to reflect new transaction data or through the passage of time). In this example, in the absence of further calibration or changes in input observability, one would expect the inception difference to be recognized over the first seven years of the contract (as years 4–10 become observable). Note that no inception difference should remain for a period in which settlement has occurred. In addition, no portion of the inception difference should remain once all the unobservable inputs become observable.
Chapter 10 — Subsequent Measurement

10.1 Introduction

ASC 820-10

35-1 The fair value measurement framework, which applies at both initial and subsequent measurement if fair value is required or permitted by another Topic, is discussed primarily in this Section. Section 820-10-30 sets out additional guidance specific to applying the framework at initial measurement. This Section is organized as follows:

a. Definition of fair value
b. Valuation techniques
c. Inputs to valuation techniques
d. Fair value hierarchy
e. Measuring fair value when the volume or level of activity for an asset or a liability has significantly decreased
f. Identifying transactions that are not orderly
g. Using quoted prices provided by third parties
h. Measuring the fair value of investments in certain entities that calculate net asset value per share (or its equivalent).

Many Codification topics require or permit the subsequent measurement of assets or liabilities at fair value (see Section 2.1.2 for more information). ASC 820-10-35 provides guidance on the subsequent measurement of items at fair value and applies to both recurring and nonrecurring measurements. This chapter discusses the subsequent-measurement requirements of ASC 820 as well as the application of these requirements to specific types of items or transactions. See Chapter 9 for discussion of initial measurements at fair value.

In addition to the guidance in ASC 820, the AICPA has issued fair value measurement guidance in the form of technical questions and answers, practice aids, and guides, including the following accounting and valuation guides:

- *Assets Acquired in a Business Combination to Be Used in Research and Development Activities.*
- *Testing Goodwill for Impairment.*
- *Valuation of Privately-Held-Company Equity Securities Issued as Compensation.*

1 Note that while such AICPA guidance constitutes an additional resource for entities to use in measuring or disclosing fair value, it is nonauthoritative, has not been approved by the FASB or SEC, and is not a substitute for the application of ASC 820.
Further, because ASC 820 is substantially converged with IFRS 13, the IASB Expert Advisory Panel report may be also be helpful for entities that apply U.S. GAAP to use in measuring or disclosing fair value (since the best practices outlined in the report were incorporated into IFRS 13). The IASB’s project summary and feedback statement for IFRS 13 describes how the report is related to IFRS 13:

In May 2008 we established a Fair Value Expert Advisory Panel that included preparers, auditors and users of financial statements, as well as regulators.

The Panel’s remit was to help us:

- review best practices in the area of valuation techniques; and
- formulate any necessary additional practice guidance on valuation methods for financial instruments and related disclosures when markets are no longer active.

In October 2008 our staff published a report summarising the Panel’s discussions. The report . . . summarised the valuation and disclosure practices undertaken by large financial institutions in the financial crisis. The requirements in IFRS 13 are consistent with that report. [Emphasis added]

10.2 Definition of Fair Value

10.2.1 General

<table>
<thead>
<tr>
<th>ASC 820-10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Definition of Fair Value</strong></td>
</tr>
<tr>
<td><strong>35-2</strong> This Topic defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.</td>
</tr>
<tr>
<td><strong>35-2A</strong> The remainder of this guidance is organized as follows:</td>
</tr>
<tr>
<td>a. The asset or liability</td>
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<tr>
<td>b. The transaction</td>
</tr>
<tr>
<td>c. Market participants</td>
</tr>
<tr>
<td>d. The price</td>
</tr>
<tr>
<td>e. Application to nonfinancial assets</td>
</tr>
<tr>
<td>f. Application to liabilities and instruments classified in a reporting entity’s shareholders’ equity</td>
</tr>
<tr>
<td>g. Application to financial assets and financial liabilities with offsetting positions in market risks or counterparty credit risk.</td>
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</tbody>
</table>

**The Fair Value Measurement Approach**

**55-1** The objective of a fair value measurement is to estimate the price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions. A fair value measurement requires a reporting entity to determine all of the following:

a. The particular asset or liability that is the subject of the measurement (consistent with its unit of account)

b. For a nonfinancial asset, the valuation premise that is appropriate for the measurement (consistent with its highest and best use)

c. The principal (or most advantageous) market for the asset or liability

d. The valuation technique(s) appropriate for the measurement, considering the availability of data with which to develop inputs that represent the assumptions that market participants would use when pricing the asset or liability and the level of the fair value hierarchy within which the inputs are categorized.
As discussed in Section 1.2, the definition of fair value is based on an exit price notion. An asset, liability, or equity instrument is measured at fair value on the basis of market-participant assumptions; such measurement is not entity-specific. Entities must consider all the characteristics of the asset, liability, or equity instrument that a market participant would consider in determining an exit price in the principal or most advantageous market. The measurement of the asset, liability, or equity instrument at fair value for recognition purposes is at the level of the unit of account, which may differ from the unit of valuation. The concepts underlying the definition of fair value are discussed in the subsections below.

10.2.2 The Asset or Liability

10.2.2.1 General

<table>
<thead>
<tr>
<th>ASC 820-10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>The Asset or Liability</strong></td>
</tr>
<tr>
<td><strong>35-2B</strong> A fair value measurement is for a particular asset or liability. Therefore, when measuring fair value a reporting entity shall take into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Such characteristics include, for example, the following:</td>
</tr>
<tr>
<td>a. The condition and location of the asset</td>
</tr>
<tr>
<td>b. Restrictions, if any, on the sale or use of the asset.</td>
</tr>
<tr>
<td><strong>35-2C</strong> The effect on the measurement arising from a particular characteristic will differ depending on how that characteristic would be taken into account by market participants. Paragraph 820-10-55-51 illustrates a restriction’s effect on fair value measurement.</td>
</tr>
<tr>
<td><strong>35-2D</strong> The asset or liability measured at fair value might be either of the following:</td>
</tr>
<tr>
<td>a. A standalone asset or liability (for example, a financial instrument or a nonfinancial asset)</td>
</tr>
<tr>
<td>b. A group of assets, a group of liabilities, or a group of assets and liabilities (for example, a reporting unit or a business).</td>
</tr>
<tr>
<td><strong>35-2E</strong> Whether the asset or liability is a standalone asset or liability, a group of assets, a group of liabilities, or a group of assets and liabilities for recognition or disclosure purposes depends on its unit of account. The unit of account for the asset or liability shall be determined in accordance with the Topic that requires or permits the fair value measurement, except as provided in this Topic.</td>
</tr>
</tbody>
</table>

Depending on the unit of account, which is generally determined in accordance with other Codification topics, the asset or liability being measured at fair value might be a stand-alone asset or liability, a group of assets, a group of liabilities, or a group of assets and liabilities. See Chapter 4 for further discussion of the unit of account.

In addition to applying the appropriate unit of account to a fair value measurement, entities may need to consider other asset-specific characteristics that affect fair value. According to ASC 820-10-35-2B, examples of potential asset-specific characteristics that may affect a fair value measurement include (1) the condition and location of the asset (see Section 10.2.5.4) and (2) restrictions on the sale or use of the asset (see Section 10.2.2.2).
10.2.2.2 Restrictions on the Sale or Use of an Asset

ASC 820-10

Example 6: Restricted Assets

55-51 The effect on a fair value measurement arising from a restriction on the sale or use of an asset by a reporting entity will differ depending on whether the restriction would be taken into account by market participants when pricing the asset. Cases A and B illustrate the effect of restrictions when measuring the fair value of an asset.

Case A: Restriction on the Sale of an Equity Instrument

55-52 A reporting entity holds an equity instrument (a financial asset) for which sale is legally or contractually restricted for a specified period. (For example, such a restriction could limit sale to qualifying investors, as may be the case in accordance with Rule 144 or similar rules of the Securities and Exchange Commission [SEC].) The restriction is a characteristic of the instrument and, therefore, would be transferred to market participants. In that case, the fair value of the instrument would be measured on the basis of the quoted price for an otherwise identical unrestricted equity instrument of the same issuer that trades in a public market, adjusted to reflect the effect of the restriction. The adjustment would reflect the amount market participants would demand because of the risk relating to the inability to access a public market for the instrument for the specified period. The adjustment will vary depending on all of the following:

a. The nature and duration of the restriction
b. The extent to which buyers are limited by the restriction (for example, there might be a large number of qualifying investors)
c. Qualitative and quantitative factors specific to both the instrument and the issuer.

55-53 As discussed in paragraph 820-10-15-5, this Topic applies for equity securities with restrictions that expire within one year that are measured at fair value in accordance with Subtopics 320-10 and 958-320.

Case B: Restrictions on the Use of an Asset

55-54 A donor contributes land in an otherwise developed residential area to a not-for-profit neighborhood association. The land is currently used as a playground. The donor specifies that the land must continue to be used by the association as a playground in perpetuity; however, the association is not restricted from selling the land. Upon review of relevant documentation (for example, legal and other), the association determines that the fiduciary responsibility to meet the donor’s restriction would not be transferred to market participants if the association sold the asset, that is, the donor restriction on the use of the land is specific to the association. Without the restriction on the use of the land by the association, the land could be used as a site for residential development. In addition, the land is subject to an easement (that is, a legal right that enables a utility to run power lines across the land). Following is an analysis of the effect on the fair value measurement of the land arising from the restriction and the easement:

a. Donor restriction on use of land. Because in this situation the donor restriction on the use of the land is specific to the association, the restriction would not be transferred to market participants. Therefore, the fair value of the land would be the higher of its fair value used as a playground (that is, the fair value of the asset would be maximized through its use by market participants in combination with other assets or with other assets and liabilities) and its fair value as a site for residential development (that is, the fair value of the asset would be maximized through its use by market participants on a standalone basis), regardless of the restriction on the use of the land by the association.

b. Easement for utility lines. Because the easement for utility lines is specific to (that is, a characteristic of) the land, it would be transferred to market participants with the land. Therefore, the fair value measurement of the land would take into account the effect of the easement, regardless of whether the highest and best use is as a playground or as a site for residential development.

55-55 The donor restriction, which is legally binding on the association, would be indicated through classification of the associated net assets and disclosure of the nature of the restriction in accordance with paragraphs 958-210-45-8 through 45-9, 958-210-50-1, and 958-210-50-3.
In some cases, it is appropriate to consider a restriction on the sale or use of an asset as a characteristic of the asset that affects its fair value. Only a legal or contractual restriction on the sale or use of an asset that is specific to the asset (an instrument-specific restriction) and that would be transferred to market participants should be incorporated into the asset's fair value measurement. Thus, an entity should consider the effect of a restriction on the sale or use of an asset that it owns only if market participants would consider such a restriction in pricing the asset because they would also be subject to the restriction if they acquired the asset. Entity-specific restrictions that would not be transferred to market participants should not be considered in the determination of the asset's fair value, since doing so would be inconsistent with the exit price notion underlying the definition of fair value. Table 10-1 gives examples of restrictions on the sale of assets and addresses whether they are instrument-specific or entity-specific. Section 5.2.3 discusses considerations related to the potential uses of nonfinancial assets that may affect the highest-and-best-use valuation premise for nonfinancial assets.

Table 10-1

<table>
<thead>
<tr>
<th>Nature of Restriction</th>
<th>Description of Restriction</th>
<th>Impact of Restriction on Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Restriction on the sale of securities offered in a private offering in accordance with SEC Rule 144 or similar rules (private placements)</td>
<td>SEC Rule 144 legally restricts the sale of certain securities to buyers that meet specified criteria.</td>
<td>As discussed in ASC 820-10-55-52, this type of restriction is a characteristic of the security and would be transferred to market participants. Therefore, the fair value measurement of the security should take this instrument-specific restriction into account. An instrument-specific restriction on a security affects a fair value measurement by the amount that a market participant would demand because of the inability to access a public market for the security for the specified period. As discussed in ASC 820-10-55-52, that amount depends on the nature and duration of the restriction, the extent to which buyers are limited by the restriction, and qualitative and quantitative factors specific to both the instrument and the issuer. Quoted prices for such securities would reflect the resale restriction; therefore, there should be no further adjustment to reflect the restriction.</td>
</tr>
<tr>
<td>Founder's shares in an IPO of equity securities</td>
<td>Founders may be contractually restricted from selling their shares for a period after an IPO. Such restrictions may be outlined in the IPO prospectus.</td>
<td>If this restriction is not embedded in the contractual terms of the shares (which it generally is not) and thus would not be transferred in a hypothetical sale of the shares, the restriction is specific to the founders and not a characteristic of the security. Therefore, the founders should not consider this restriction in determining fair value.</td>
</tr>
</tbody>
</table>
The determination of whether a contractual or legal restriction on the sale or use of an asset is instrument-specific or entity-specific is sometimes straightforward; other times, an entity may need to exercise judgment or consult a legal specialist in making this determination.

### 10.2.3 The Transaction

**ASC 820-10**

#### The Transaction

**35-3** A fair value measurement assumes that the asset or liability is exchanged in an orderly transaction between market participants to sell the asset or transfer the liability at the measurement date under current market conditions.

**35-5** A fair value measurement assumes that the transaction to sell the asset or transfer the liability takes place either:

- a. In the principal market for the asset or liability
- b. In the absence of a principal market, in the most advantageous market for the asset or liability.

**35-5A** A reporting entity need not undertake an exhaustive search of all possible markets to identify the principal market or, in the absence of a principal market, the most advantageous market, but it shall take into account all information that is reasonably available. In the absence of evidence to the contrary, the market in which the reporting entity normally would enter into a transaction to sell the asset or to transfer the liability is presumed to be the principal market or, in the absence of a principal market, the most advantageous market.

**35-6** If there is a principal market for the asset or liability, the fair value measurement shall represent the price in that market (whether that price is directly observable or estimated using another valuation technique), even if the price in a different market is potentially more advantageous at the measurement date.
ASC 820-10 (continued)

35-6A The reporting entity must have access to the principal (or most advantageous) market at the measurement date. Because different entities (and businesses within those entities) with different activities may have access to different markets, the principal (or most advantageous) market for the same asset or liability might be different for different entities (and businesses within those entities). Therefore, the principal (or most advantageous) market (and thus, market participants) shall be considered from the perspective of the reporting entity, thereby allowing for differences between and among entities with different activities.

35-6B Although a reporting entity must be able to access the market, the reporting entity does not need to be able to sell the particular asset or transfer the particular liability on the measurement date to be able to measure fair value on the basis of the price in that market.

35-6C Even when there is no observable market to provide pricing information about the sale of an asset or the transfer of a liability at the measurement date, a fair value measurement shall assume that a transaction takes place at that date, considered from the perspective of a market participant that holds the asset or owes the liability. That assumed transaction establishes a basis for estimating the price to sell the asset or to transfer the liability.

As discussed in ASC 820-10-35-5, in a fair value measurement, it is assumed that an orderly transaction to sell the asset or transfer the liability has occurred in the principal market for the asset or liability (or, in the absence of a principal market, the most advantageous market). While a fair value measurement is not entity-specific, the principal (or most advantageous) market for the asset or liability is determined from the perspective of the entity estimating fair value for recognition or disclosure purposes. See Chapter 6 for discussion of the concept of the principal or most advantageous market. Also see Example 10-9, which illustrates how to identify the most advantageous market for a nonfinancial asset.

10.2.4 Market Participants

ASC 820-10

Market Participants

35-9 A reporting entity shall measure the fair value of an asset or a liability using the assumptions that market participants would use in pricing the asset or liability, assuming that market participants act in their economic best interest. In developing those assumptions, a reporting entity need not identify specific market participants. Rather, the reporting entity shall identify characteristics that distinguish market participants generally, considering factors specific to all of the following:

a. The asset or liability
b. The principal (or most advantageous) market for the asset or liability
c. Market participants with whom the reporting entity would enter into a transaction in that market.

To reflect an exit price in accordance with the definition and objective of a fair value measurement, an asset or liability must be measured on the basis of assumptions that market participants would use in pricing the asset or liability. See Chapter 7 for further discussion of market-participant assumptions and Section 10.4 for information about inputs into a valuation technique.
10.2.5 The Price

10.2.5.1 General

ASC 820-10

The Price

35-9A Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market conditions (that is, an exit price) regardless of whether that price is directly observable or estimated using another valuation technique.

35-9B The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. Transaction costs shall be accounted for in accordance with other Topics. Transaction costs are not a characteristic of an asset or a liability; rather, they are specific to a transaction and will differ depending on how a reporting entity enters into a transaction for the asset or liability.

35-9C Transaction costs do not include transportation costs. If location is a characteristic of the asset (as might be the case, for example, for a commodity), the price in the principal (or most advantageous) market shall be adjusted for the costs, if any, that would be incurred to transport the asset from its current location to that market.

In the principal (or most advantageous) market, the price used to measure the fair value of an asset, liability, or instrument classified in an entity’s stockholders’ equity is determined as of the measurement date under current market conditions. This price should not be adjusted for transaction costs but may be adjusted for transportation costs.

10.2.5.2 Subsequent Information and Events

ASC 820-10-35-9A indicates that a fair value measurement represents “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction . . . at the measurement date under current market conditions.” In estimating fair value, an entity should develop inputs on the basis of the assumptions that market participants would make as of the measurement date, provided that such participants performed usual and customary due diligence procedures. In making assumptions about the inputs that market participants would use in estimating fair value, an entity is responsible for analyzing and considering “any relevant subsequent events and information to assess whether the fair value measurement reflects all relevant information and assumptions that market participants would have considered under the current conditions at the measurement date.”

Relevant information related to the assumptions about the inputs used to estimate fair value may include general market and economic data, industry data, and investment-specific data. Relevant information obtained after the measurement date but before the financial statements are issued (or available to be issued) may serve as additional evidence of the assumptions that market participants would have made in developing inputs as of the measurement date after making usual and customary due diligence efforts. Conversely, such information may represent information that market participants would not have considered as of the measurement date after making these efforts. In all cases, a fair

2 The definition of a market participant in ASC 820-10 refers to parties that have a “reasonable understanding about the asset or liability and the transaction using all available information, including information that might be obtained through due diligence efforts that are usual and customary.” ASC 820-10-35-54A notes that “[a] reporting entity need not undertake exhaustive efforts to obtain information about market participant assumptions. However, a reporting entity shall take into account all information about market participant assumptions that is reasonably available.”

3 Quoted from the Background Information and Basis for Conclusions of ASU 2012-07. While this ASU specifically applies to impairment assessments of unamortized film costs, in accordance with ASC 855 and paragraph 41 of AICPA and PCAOB AU Section 328, the requirement to consider all relevant information that is obtained after the measurement date but before the financial statements are issued (or available to be issued) is broadly applicable to all fair value measurements.
value measurement as of the measurement date should incorporate assumptions about risk, including risks inherent in (1) a particular valuation technique and (2) the inputs to the valuation technique.\footnote{See ASC 820-10-35-54 in \textit{Section 10.4.2}.} If uncertainty is inherent in the inputs used to estimate fair value as of the measurement date, the entity cannot disregard such uncertainty in estimating fair value even if the uncertainty is not resolved until after the measurement date. In some cases, it may be difficult to determine the appropriate risk adjustments that market participants may make to reflect the uncertainty inherent in the inputs used in a fair value measurement; however, the degree of difficulty is not a sufficient basis for excluding a risk adjustment.\footnote{See ASC 820-10-35-54E in \textit{Section 10.6.1}.}

In evaluating how to consider relevant information obtained after the measurement date in estimating fair value as of the measurement date, an entity should consider the guidance in ASC 855, which distinguishes between recognized and unrecognized subsequent events. AU Section 560 defines recognized subsequent events as those that “provide additional evidence with respect to conditions that existed at the date of the balance sheet and affect the estimates inherent in the process of preparing financial statements.” Nonrecognized subsequent events, on the other hand, are those that “provide evidence with respect to conditions that did not exist at the date of the balance sheet being reported on but arose subsequent to that date.” Entities should adjust their financial statements only to reflect the impact of recognized subsequent events. For nonrecognized subsequent events, entities should evaluate the completeness of their financial statement disclosures.

Furthermore, auditors should consider paragraph 42 of AU Section 328, which states:

Some subsequent events or transactions may reflect changes in circumstances occurring after the balance-sheet date and thus do not constitute appropriate evidence of the fair value measurement at the balance-sheet date (for example, the prices of actively traded marketable securities that change after the balance-sheet date). When using a subsequent event or transaction to substantiate a fair value measurement, the auditor considers only those events or transactions that reflect circumstances existing at the balance-sheet date.

In applying ASC 855 and paragraph 42 of AU Section 328 to a fair value measurement, an entity must consider the following questions:\footnote{Note that this framework for evaluating subsequent information and events would not apply to (1) investments that are measured at NAV per share in accordance with the practical expedient in ASC 820-10-35-59 through 35-62 or (2) Level 1 inputs.}

1. \textbf{Does the information obtained after the measurement date constitute evidence of a condition that existed as of the measurement date?}

If the information obtained after the measurement date constitutes evidence of a condition that existed as of the measurement date, go to question 2. If the information serves as evidence of a condition that did not exist as of the measurement date, the information obtained after the measurement date represents a nonrecognized subsequent event. Nonrecognized subsequent events do not result in adjustments of the financial statements; however, disclosures may be required under ASC 855-10-50-2 and 50-3.

2. \textbf{Does the information obtained after the measurement date represent information that would have been available to market participants as of the measurement date (under an assumption that market participants performed usual and customary due diligence efforts)?}

If the information obtained by an entity after the measurement date would have been available to market participants as of the measurement date, the entity should directly consider the information in developing the inputs into the fair value measurement as of the measurement date. If, however, the information obtained by the entity after the measurement date reflects only the resolution of a particular uncertainty that existed as of the measurement date, the
information itself should not be used with certainty as an input into the fair value measurement as of the measurement date. However, the entity should ensure that the estimation of fair value as of the measurement date appropriately includes assumptions about risks related to the uncertainty that existed as of the measurement date.

The summary section of ASU 2012-07 further elaborates on how an entity considers information obtained after the measurement date that resolves an uncertainty that existed as of the measurement date:

[An] entity should include, in a valuation model, assumptions that market participants would have made about uncertainty in timing and amount of cash flows as of the measurement date. To the extent that uncertainties are resolved or other information becomes known after the balance sheet date, but before the financial statements are issued or available to be issued, such effects should not be incorporated with certainty into the fair value measurement as of the balance sheet date unless market participants would have made such assumptions.

The examples below illustrate the application of the guidance discussed above.

### Example 10-1

**Information Not Available as of the Measurement Date**

Entity A holds marketable securities and records them at fair value in its balance sheet on the basis of a quoted market price. As of A’s year-end (i.e., the measurement date), these securities had a quoted price per share of $150. After the measurement date, the securities’ quoted price per share dropped to $120. In this example, it is assumed that the decline occurs after the measurement date; events that occur after market close but before the end of the measurement date are not considered subsequent events.

The decline in the quoted price is a nonrecognized subsequent event because it represents information that market participants would not have had as of the measurement date; therefore, A should not adjust its fair value measurement of the marketable securities as of the measurement date. However, if the investment in marketable securities or decline in their fair value is significant to A, A should consider the decline in determining whether its financial statement disclosures are adequate.

### Example 10-2

**Information Both Available and Not Available as of the Measurement Date**

Entity B holds a limited partnership interest in Partnership Z, which is a nonpublic entity that invests in real estate in southeast Asia (the “investment”). Entity B recognizes the investment at fair value through earnings in its financial statements. Entity B’s fiscal year-end is December 31, 20X5, and it issues its financial statements on February 28, 20X6. Entity B receives a financial information package from the general partner of Z on a 30-day lag. The financial information received from Z includes financial statements as of the prior month-end and updated projections of Z’s future cash flows (the “cash flow projections”). Entity B estimates the fair value of Z by using a present value technique that incorporates the cash flow projections received from Z, which represent a significant unobservable input into the valuation technique. As part of its year-end closing process, B uses the cash flow projections received from Z as part of the November 30, 20X5, financial information package (the “original projections”) to estimate the fair value of the investment as of the December 31, 20X5, measurement date. On February 1, 20X6, B receives the December 31, 20X5, financial information package from Z, which includes revised cash flow projections (the “updated cash flow projections”). The updated cash flow projections are significantly revised downward from the original cash flow projections. The negative revisions in both the amount and timing of Z’s estimated future cash flows are primarily attributable to two factors: (1) adverse economic developments in the general real estate market in southeast Asia that occurred in December 20X5 and (2) a discrete decision made by the general partner of Z on January 15, 20X6, to abandon two real estate projects in process. In the analysis below, it is assumed that as part of the usual and customary due diligence procedures that would be performed before a decision is made to invest in Z, market participants would (1) be knowledgeable about general economic conditions in the southeast Asian real estate market that would affect Z and (2) have access to the same financial information that B receives from Z. The general partner of Z would not, however, provide access to confidential information that is not made available to existing investors in Z.
Example 10-2 (continued)

The receipt of the updated cash flow projections from Z constitutes evidence of both a condition that existed as of the December 31, 20X5, measurement date (i.e., the impact of adverse economic developments in the southeast Asian real estate market) and a condition that did not exist as of the December 31, 20X5, measurement date (i.e., the discrete decision to abandon two real estate projects in process). In determining a transaction price for the investment in Z as of the December 31, 20X5, measurement date, market participants would not have had access to the updated cash flow projections, although they would have been knowledgeable of the fact that deteriorating economic conditions in the southeast Asian real estate market would affect Z’s future business prospects. Therefore, while it would be inappropriate to directly incorporate the updated cash flow projections as an input into the valuation technique, B should appropriately incorporate assumptions about the risks that market participants would consider inherent in the original projections (including the compensation for bearing such risks). Given the usual and customary due diligence procedures that market participants would perform in determining a transaction price for the investment, the assumptions market participants would make about the risks inherent in the original cash flow projections would be expected to include risk adjustments pertaining to the adverse economic developments in the southeast Asian real estate market in December 20X5 as well as the execution risks involved in Z’s real estate projects in process. Market participants would have incorporated assumptions regarding the risks inherent in the original cash flow projections on the basis of judgments regarding the uncertainty in the timing and amounts of cash flows as of the measurement date without the benefit of any resolution of these uncertainties that may have been provided once the updated cash flow projections were made available.

Example 10-3

Observable Transaction After the Measurement Date

Entity C holds a common equity ownership interest in a private company, X, that C recognizes at fair value through earnings in its financial statements. Entity C’s fiscal year-end is December 31, 20X5, and it issues its financial statements on February 28, 20X6. In performing its year-end closing, C used both the market approach and the income approach to estimate the fair value of its investment in X. For both techniques, significant unobservable (Level 3) inputs were required because no observable market transactions for the asset occurred during the reporting period and no comparable market information was available. (See Section 10.3.2 for a discussion of the use of multiple valuation techniques.)

An observable market transaction in X’s common equity occurred between unrelated entities on January 15, 20X6. (Note that as discussed in Section 10.4.1, ASC 820-10-35-36 requires entities to maximize the use of relevant observable inputs (i.e., Level 1 and Level 2 inputs that do not need to be significantly adjusted) and minimize the use of unobservable inputs in their valuation techniques.) Entity C should evaluate significant differences between (1) its estimate of the fair value of its investment in X under the market approach and income approach and (2) the observable transaction price. The subsequent transaction and related information may constitute additional evidence of the fair value of C’s investment in X as of the measurement date, indicating that an adjustment would be appropriate.

However, in evaluating whether the subsequent transaction price is relevant to the fair value of C’s investment in X as of the measurement date, C should consider whether (1) significant events (e.g., market changes or changes in the investee’s business, including the industry in which X operates) have occurred between the measurement date and the subsequent transaction date and (2) the transaction represents an orderly transaction (as opposed to a forced liquidation or distressed sale). If significant events have occurred after the measurement date or C is unable to determine whether the transaction represents an orderly transaction, C should place less weight on the subsequent market transaction. In addition, the further from the measurement date that the market transaction takes place, the less weight C should place on the input. If it is determined that the subsequent transaction represented an orderly transaction that provides relevant information regarding the fair value of C’s investment in X as of the measurement date, C should consider whether it needs to adjust this input for the effect of significant events that occurred after the measurement date. See Section 10.7 for more information about identifying whether transactions are orderly transactions.
Example 10-3 (continued)

Such transactions may also represent an opportunity for an entity to calibrate its valuation technique (including the significant inputs into the valuation technique). In doing so, the entity may become aware that inputs it developed on the basis of its own assumptions differ significantly from inputs developed on the basis of market-participant assumptions. ASC 820-10-35-24C addresses such calibration:

Calibration ensures that the valuation technique reflects current market conditions, and it helps a reporting entity to determine whether an adjustment to the valuation technique is necessary (for example, there might be a characteristic of the asset or liability [or instrument classified within an entity’s shareholders’ equity] that is not captured by the valuation technique). After initial recognition, when measuring fair value using a valuation technique or techniques that use unobservable inputs, a reporting entity shall ensure that those valuation techniques reflect observable market data (for example, the price for a similar asset or liability [or own equity instrument]) at the measurement date.

10.2.5.3 Transaction Costs

10.2.5.3.1 General

**ASC 820-10 — Glossary**

**Transaction Costs**

The costs to sell an asset or transfer a liability in the principal (or most advantageous) market for the asset or liability that are directly attributable to the disposal of the asset or the transfer of the liability and meet both of the following criteria:

a. They result directly from and are essential to that transaction.

b. They would not have been incurred by the entity had the decision to sell the asset or transfer the liability not been made (similar to costs to sell, as defined in paragraph 360-10-35-38).

As noted in ASC 820-10-35-9B, a fair value measurement does not include the effects of transaction costs. As a result, as discussed in ASC 820-10-30-3A(c), the transaction price (i.e., the price paid) may not represent fair value at initial recognition. Because transaction costs may be embedded in the price paid (received) for an asset (liability), entities should use judgment in identifying transaction costs. Transaction costs are recognized in earnings as incurred when they are related to an item that is subsequently recognized at fair value, with changes in fair value reported in earnings.7

An entity should consider transaction costs in determining the most advantageous market in which to measure fair value when there is no principal market for an asset, liability, or equity instrument. Such costs may influence the net proceeds received or paid in a transaction and therefore the selection of the most advantageous market in which to transact. However, once the most advantageous market is determined, transaction costs do not result in adjustments to the price in this market. See Section 10.2.5.3.2 for discussion of the accounting for transaction costs.

7 See Section 12.3.1.2 for discussion of the accounting for up-front costs when the FVO is elected for an eligible item.
Furthermore, although ASC 820-10-35-9B indicates that the price used to measure fair value is not adjusted for transaction costs, when an entity uses a discounted cash flow technique to measure the fair value of a nonfinancial asset, the entity may appropriately include the costs of disposing of the asset when these costs are one of the cash flow assumptions that market participants would use in pricing the asset (see Example 10-4 for an illustration). However, this approach would not apply to a fair value measurement of a financial asset or financial liability.  

**Example 10-4**

**Accounting for Selling Costs When a Discounted Cash Flow Model Is Used to Measure the Fair Value of a Nonfinancial Asset**

Entity D uses a discounted cash flow model to measure the fair value of an investment property. In doing so, D develops a 10-year cash flow projection for the property's operations, with an assumed sale at the end of the 10-year period because D believes that this is how market participants would price the investment property and has no knowledge of any available evidence to the contrary. The net cash inflow from the assumed sale would include the impact of selling costs (i.e., selling costs would be subtracted from the cash inflow of the estimated sales price). In measuring the fair value of its investment property, D would use an appropriate rate to discount the resulting cash flows to present value.

Transaction costs differ from transportation and installation costs. See Section 10.2.5.4 for discussion of transportation and installation costs. Also see Example 10-9, which illustrates how an entity would consider transaction, transportation, and installation costs in determining the most advantageous market and the fair value of a nonfinancial asset.

### 10.2.5.3.2 Accounting for Transaction Costs

Entities should consider other Codification topics in accounting for transaction costs. Although transaction costs are recognized in earnings as incurred for items subsequently measured at fair value through earnings, such recognition may not be appropriate when an item is subsequently measured by using an attribute other than fair value through earnings. For example, when an asset is recognized at amortized cost, it may be appropriate to capitalize transaction costs as part of the cost of the asset.

Furthermore, some Codification topics require the subsequent recognition of an asset at fair value less costs to sell (i.e., the subsequent measurement of the asset is reduced by anticipated transaction costs related to selling the asset). Thus, both the transaction costs incurred to acquire the asset and the transaction costs that will be incurred to sell the asset may be recognized in earnings while the entity owns the asset.

The subsections below discuss other Codification topics (not all-inclusive) that address the accounting for transaction costs.

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8 See Section 10.10.8.2 for discussion of the fair value measurement of a contract termination cost liability associated with an operating lease when the liability is measured on the basis of the remaining future rentals that will be incurred without economic benefit reduced by the estimated sublease rentals that could be reasonably obtained for the leased property. In this example, the liability is not considered a financial liability.
Chapter 10 — Subsequent Measurement

10.2.5.3.2.1 Investments in Debt Securities

Under ASC 320, an entity may classify investments in debt securities as held to maturity, available for sale, or trading. Table 10-2 discusses the accounting for transaction costs incurred when a debt security is acquired.

### Table 10-2

<table>
<thead>
<tr>
<th>Classification of Security</th>
<th>Accounting for Transaction Costs</th>
</tr>
</thead>
</table>
| Held to maturity           | Capitalized. In accordance with ASC 310-20-15-2 and 15-3, nonrefundable fees and costs associated with acquiring debt securities classified as held to maturity are within the scope of ASC 310-20. ASC 310-20-30-5 states that the “initial investment in a purchased loan or group of loans shall include the amount paid to the seller plus any fees paid or less any fees received.” Because transaction costs associated with the acquisition of held-to-maturity debt securities are within the scope of ASC 320, fees paid to a third party that are directly related to the acquisition (e.g., brokerage fees paid to a broker-dealer) would be capitalized as part of the original carrying amount. In accordance with ASC 310-20, entities should separately expense any other costs incurred in connection with acquiring securities (e.g., internal costs, portfolio management fees, investment consultation, or due diligence costs paid to an adviser).

Held-to-maturity debt securities are subsequently measured at amortized cost and are subject to evaluation for impairment. |

| Available for sale         | Capitalized initially. In accordance with ASC 310-20-15-2 and 15-3, nonrefundable fees and costs associated with acquiring debt securities classified as available for sale are within the scope of ASC 310-20. ASC 310-20-30-5 states that the “initial investment in a purchased loan or group of loans shall include the amount paid to the seller plus any fees paid or less any fees received.” Because transaction costs associated with the acquisition of available-for-sale debt securities are within the scope of ASC 320, fees paid to a third party that are directly related to the acquisition (e.g., brokerage fees paid to a broker-dealer) would be capitalized as part of the original carrying amount. In accordance with ASC 310-20, entities should separately expense any other costs incurred in connection with acquiring securities (e.g., internal costs, portfolio management fees, investment consultation, or due diligence costs paid to an adviser).

An entity must subsequently measure debt securities classified as available for sale at fair value, with changes in fair value recognized in OCI (provided that there is no impairment). This fair value should not include any transaction costs because ASC 820 indicates that such costs are not a characteristic of an asset or liability measured at fair value. Therefore, entities will immediately recognize an unrealized loss in OCI after the purchase of a debt security classified as available for sale. Given the security’s classification as available for sale, such a loss will be reported in AOCI unless the security is subsequently impaired and measured at fair value on the basis of the entity’s conclusion that it is more likely than not that the security will be sold or that there is an intent to sell it. |

| Trading                    | Expensed as incurred. ASC 820 indicates that transaction costs are not a characteristic of an asset or liability measured at fair value. ASC 310-20-15-3(c) states that ASC 310-20 does not apply to securities that are subsequently measured at fair value through earnings. |
10.2.5.3.2.2 Investments in Equity Securities Not Subject to the Equity Method

Unless the measurement alternative in ASC 321-10-35-2 is applied or the investment qualifies for the equity method of accounting, investments in equity securities must be initially and subsequently recognized at fair value, with changes in fair value reported in earnings. Since ASC 820 indicates that transaction costs are not a characteristic of an asset or liability measured at fair value, transaction costs incurred to acquire an equity security that is not measured under the measurement alternative in ASC 321-10-35-2 are immediately expensed. See Example 10-5 for an illustration of this concept.

ASC 321-10-35-2 indicates that when the measurement alternative is applied to an equity security without a readily determinable fair value, that security is measured at “cost minus impairment, if any,” and adjustments are also made for “observable price changes in orderly transactions for the identical or a similar investment of the same issuer.” Thus, securities measured according to this measurement alternative are initially measured at the transaction price, which includes incremental direct costs related to acquiring the security (i.e., transaction costs). However, these capitalized transaction costs would be subsequently expensed in earnings upon (1) a remeasurement event under ASC 321, which includes an impairment or an observable price change (as indicated in Section 2.3.2.1.2, such a change represents a fair value measurement accounted for under ASC 820); (2) a sale of the security; or (3) a reclassification of the security to fair value through earnings (see Section 12.3.2.1).

Example 10-5

Acquisition of Equity Security Subsequently Accounted for at Fair Value

Entity E acquires an investment in an exchange-traded equity security on December 31, 20X7. The asset will be accounted for at fair value through earnings on a recurring basis in accordance with ASC 321. Entity E paid $100 for the security (which was also the security's closing price), plus a $1 broker commission, for a total transaction price of $101. Entity E transacted in its principal market for the security. However, in accordance with ASC 820-10-30-3A(c), E determines that the transaction price does not represent fair value at initial recognition because of the transaction costs. The closing price on December 31, 20X7, is $100. If E were to subsequently sell the security, it would incur a $1 broker commission.

The fair value of the security as of the December 31, 20X7, reporting date is the security's $100 closing price. Since ASC 321 does not indicate otherwise, E should record a $1 expense for the broker commission paid to acquire the security. The broker commission is not a characteristic of the security and does not add value to it. Transaction costs are a separate unit of account and therefore do not enter into the fair value measurement of the security. The $1 broker commission indicates that the transaction price of $101 is not fair value at inception. Another market participant would not reimburse E for the broker commission; instead, it would pay B the closing market price of $100 for the security. In a manner consistent with ASC 820-10-35-9B and Example 4 in ASC 820-10-55-42 through 55-45A, E should not adjust the security for the $1 broker commission it would incur to sell the security. In other words, E should not write down the security to $99 (the net proceeds it would receive upon selling the security).

10.2.5.3.2.3 Investment Securities Owned by an Investment Company

ASC 946-320-35-1 states that “[a]n investment company shall measure investments in debt and equity securities subsequently at fair value.” In addition, ASC 946-320-30-1 states that “[a]n investment company shall initially measure its investments in debt and equity securities at their transaction price. The transaction price shall include commissions and other charges that are part of the purchase transaction.” According to this guidance, investment companies initially recognize investments in debt and equity securities at the transaction price, including related commissions and other direct costs incurred in connection with acquisition of the securities (i.e., an entry price and not fair value), and subsequently measure the investments at fair value under ASC 820. If any other potential differences between entry and exit prices are ignored, the capitalization of transaction costs into the initial measurement of investment securities by investment companies will result in a loss on initial
recognition. For example, assume that Mutual Fund X purchases a publicly traded equity security for $99 immediately before the market closing (the fair value is therefore also $99). Also assume that X incurred a $1 commission in purchasing the security. Under ASC 946, the initial cost basis is $100 ($99 plus the $1 transaction cost). The fair value would be $99; therefore, a $1 loss would be recognized on the acquisition date. This loss on initial recognition is presented as a “net change in unrealized appreciation (depreciation) on investments” rather than as a separate expense in the investment company’s statement of operations.

Some have questioned whether ASC 820’s exit price notion and guidance indicating that transaction costs are not a characteristic of an asset measured at fair value conflict with the guidance in ASC 946-320-30-1. The implication is that investment companies would not be permitted to present transaction costs as part of the net change in unrealized appreciation (depreciation) on investments. However, we believe that investment companies that apply ASC 946 should present commissions and other charges that are directly related to the acquisition of investment securities in the net change in unrealized appreciation (depreciation) on investments. ASC 820-10-35-9B states, in part: “Transaction costs shall be accounted for in accordance with other Topics.” ASC 946-320-30-1 specifies that the initial amount recorded for investment purchases “shall include commissions and other charges that are part of the purchase transaction.” ASC 820 does not affect this guidance. Accordingly, ASC 946 continues to require investment companies to include commissions and other charges incurred as part of securities purchase transactions in the net change in unrealized appreciation (depreciation) on investments. After initial recognition, an investment company measures its investment at the exit price in accordance with ASC 820. The difference between the initial recognized amount and subsequent fair value measurement would be presented as a “net change in unrealized appreciation (depreciation) on investments” rather than as a separate expense in the statement of operations.

10.2.5.3.2.4 Plan Assets of Pension and Other Postretirement Benefit Plans

Unlike other fair value measurements, the fair value measurement of investments held by a pension or other postretirement plan should be reduced by the costs of disposing of the assets. ASC 715-30-35-50 states, in part:

The fair value of an investment shall be reduced by brokerage commissions and other costs normally incurred in a sale if those costs are significant (similar to fair value less cost to sell).

Example 10-6 illustrates the accounting for transaction costs of a defined benefit pension plan.

**Example 10-6**

**Transaction Costs of Pension Plan**

Entity F’s defined benefit pension plan owns a suburban office complex with an appraised value of $18 million. To recognize this real estate property in accordance with ASC 715-30-35-50, F would need to consider the estimated transaction costs (real estate broker fees) that would be incurred to dispose of the property. If the real estate broker fee is 6 percent of the transaction price ($1,080,000), the suburban office complex would be recognized at $16,920,000.

10.2.5.3.2.5 Assets Measured at Lower of Cost or Fair Value

Under certain Codification topics, assets, asset groups, or disposal groups must be measured at the lower of cost or fair value. Those Codification topics specify whether the fair value measurement should be reduced for transaction costs. For example, under ASC 310-10-35-48, nonmortgage loans classified as HFS must be reported at the lower of amortized cost or fair value. ASC 310-10-35-48 does not indicate that fair value should be reduced for anticipated costs to sell. Conversely, under ASC 310-10-
35-23 (or ASC 326-20-35-4 for entities that have adopted ASU 2016-13), when an HFI classified loan receivable is measured for impairment on the basis of the fair value of the collateral and repayment of the loan depends on the sale of the collateral, impairment measurement must be based on fair value less costs to sell. With respect to nonfinancial assets, ASC 360-10-35-17 requires that an impairment loss on a long-lived asset (or asset group) classified as held and used be measured on the basis of fair value without adjustment for costs to sell; however, an impairment loss on a disposal group is measured on the basis of fair value less costs to sell in accordance with ASC 360-10-35-40.

### 10.2.5.4 Transportation and Installation Costs

<table>
<thead>
<tr>
<th>ASC 820-10 — Glossary</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Transportation Costs</strong></td>
</tr>
<tr>
<td>The costs that would be incurred to transport an asset from its current location to its principal (or most advantageous) market.</td>
</tr>
</tbody>
</table>

As noted above, the ASC master glossary defines transportation costs (e.g., freight costs, handling fees, or other similar costs) as the costs of moving an asset “from its current location to its principal (or most advantageous) market.” Like transaction costs, transportation costs may be embedded in the transaction price for an asset. However, transportation costs are treated differently than transaction costs for fair value measurement purposes.

Under ASC 820, an entity that is measuring fair value must consider the characteristics of an asset or liability, which, in the case of a nonfinancial asset (e.g., a commodity), may include the asset’s physical location. Thus, in determining the fair value of an asset for which location is a characteristic, an entity may need to adjust an observable price or input for the costs that would be incurred to transport the asset from its current location to the principal (or most advantageous) market. Similarly, in determining the fair value of a nonfinancial asset that must be customized or configured to be placed into service and ready for use, an entity may need to adjust an observable price or input to reflect the associated installation costs. Such an adjustment is appropriate when the degree of customization or configuration (i.e., installation) is a characteristic of the asset.

Examples 10-7 and 10-8 illustrate how transportation costs may be added to or subtracted from a quoted price to arrive at a fair value measurement (e.g., how an observable market price may be adjusted to arrive at fair value in the principal or most advantageous market for an asset). While these examples focus on assets, a contract that is an asset from one party’s perspective will represent a liability from the counterparty’s perspective. In addition, note that these examples do not address whether it is appropriate to recognize inventories at fair value under U.S. GAAP.

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9 For example, ASC 820-10-55-3(b) indicates that if an entity determines a fair value measurement for a machine that is installed and ready for use by using an observed price for a similar machine that is not installed or ready for use, the observed price should be “adjusted for transportation and installation costs so that the fair value measurement reflects the current condition and location of the machine (installed and configured for use).” Similarly, if an entity is estimating the fair value of a machine that is not installed and ready to use by using an observed price for a similar machine that is installed and ready for use, the observed price may need to be adjusted to reflect the fair value of the uninstalled machine. Thus, like the adjustments for transportation costs illustrated in Examples 10-7 and 10-8, adjustments for installation costs could be additive or subtractive.
Chapter 10 — Subsequent Measurement

Example 10-7

**Location Is a Subtractive Input**

Entity G has commodity inventory at Location 1. In performing its fair value measurement, G determines that Location 2 is the principal market for sale of this inventory. Location 2 is an active market for which pricing quotes are readily accessible. Entity G observes a price of $100 per unit of inventory at Location 2. Entity G determines that transporting the inventory from Location 1 to Location 2 would cost $5 per unit of inventory. The fair value of the inventory at its current location would thus be $95 per unit (i.e., $100 per unit at location 2 less $5 per unit to bring the asset to the principal market at Location 2).

**Entity G’s analysis (per unit):**

<table>
<thead>
<tr>
<th>Location 2:</th>
<th>Location 1:</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Principal market</td>
<td>• Commodity inventory</td>
</tr>
<tr>
<td>• Active market with observable prices</td>
<td>$5 transportation</td>
</tr>
<tr>
<td>Market price = $100</td>
<td></td>
</tr>
</tbody>
</table>

**Fair value calculation**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market price at principal market</td>
<td>$100</td>
</tr>
<tr>
<td>Transportation costs</td>
<td>(5)</td>
</tr>
<tr>
<td>Fair value at inventory location</td>
<td>$95</td>
</tr>
</tbody>
</table>

Example 10-8

**Location Is an Additive Input**

Entity H has commodity inventory at Location 1. In performing its fair value measurement, H determines that Location 1 is its principal market for sale of this inventory. However, no recent observable pricing information is available at Location 1. Accordingly, H uses a valuation technique to determine the fair value of the inventory at Location 1 on the basis of quoted prices at Location 2, from which a more recent price quote can be obtained. The valuation technique is used to adjust the quoted price at Location 2 for the cost of transportation from Location 2 to Location 1. As in Example 10-7, the current price at Location 2 is $100 per unit of inventory. The transportation cost from Location 2 to Location 1 is $5 per unit of inventory. Entity H validates its valuation technique on the basis of past market transactions at Location 1. The fair value of the inventory at its current location would thus be $105 per unit (i.e., $100 per unit at Location 2 plus $5 per unit to bring the asset to H’s principal market at Location 1).

**Entity H’s analysis (per unit):**

<table>
<thead>
<tr>
<th>Location 2:</th>
<th>Location 1:</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Active market with observable prices</td>
<td>• Commodity inventory</td>
</tr>
<tr>
<td>• Principal market</td>
<td>$5 transportation</td>
</tr>
<tr>
<td>Market price = $100</td>
<td></td>
</tr>
</tbody>
</table>

**Fair value calculation**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market price at principal market</td>
<td>$100</td>
</tr>
<tr>
<td>Transportation costs</td>
<td>5</td>
</tr>
<tr>
<td>Fair value at inventory location</td>
<td>$105</td>
</tr>
</tbody>
</table>
Example 10-9 illustrates how an entity would consider transaction, transportation, and installation costs in determining the most advantageous market and fair value for a nonfinancial asset.

**Example 10-9**

**Transaction, Transportation, and Installation Costs for a Nonfinancial Asset**

Entity I owns an uninstalled machine for which it is measuring fair value for impairment purposes. Entity I has determined the following:

- There are observable prices for the machine on an installed basis in Market A and Market B.
- Entity I has access to transact in both markets, although neither market is I’s principal market.
- To sell the machine in either market, I would need to transport the machine to the market and configure and install the machine so that it is ready for use.
- Entity I would also incur a commission (i.e., a transaction cost) to sell the machine on an installed basis in either market.
- The observable prices and costs of selling the machine in Markets A and B on an installed basis are as follows:

<table>
<thead>
<tr>
<th></th>
<th>Market A</th>
<th>Market B</th>
</tr>
</thead>
<tbody>
<tr>
<td>Price</td>
<td>$28</td>
<td>$26</td>
</tr>
<tr>
<td>Transportation costs</td>
<td>4</td>
<td>1</td>
</tr>
<tr>
<td>Installation costs</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Transaction costs</td>
<td>1</td>
<td>3</td>
</tr>
</tbody>
</table>

ASC 820 specifies that an entity should make an adjustment for transportation and installation costs when measuring the fair value of an asset if location and condition are characteristics of the asset. Transaction costs are not part of a fair value measurement, but they do affect the determination of the most advantageous market when there is no principal market for an asset. (As discussed in Section 10.2.5.3.1, when the fair value of a nonfinancial asset is calculated by using a discounted cash flow technique, the cost of disposing of the asset, which represents a type of transaction cost, may reduce the cash flows used in the model to estimate fair value. However, that guidance does not apply to this example.)

Under ASC 820, the fair value of the machine is $22 in Market A ($28 observable price less the $4 transportation costs and $2 installation costs that would be incurred for I to obtain that price) and $23 in Market B ($26 observable price less the $1 transportation costs and $2 installation costs that I would incur to obtain that price). The net proceeds would be $21 in Market A (fair value of $22 less $1 transaction costs) and $20 in Market B (fair value of $23 less $3 transaction costs). Because the price in Market A results in greater net proceeds, from I’s perspective, Market A is the most advantageous market for the machine; therefore, the fair value of the machine is $22.

### 10.2.6 Application to Nonfinancial Assets

**ASC 820-10**

**Highest and Best Use for Nonfinancial Assets**

35-10A A fair value measurement of a nonfinancial asset takes into account a market participant’s ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.
The highest and best use of a nonfinancial asset takes into account the use of the asset that is physically possible, legally permissible, and financially feasible, as follows:

a. A use that is physically possible takes into account the physical characteristics of the asset that market participants would take into account when pricing the asset (for example, the location or size of a property).

b. A use that is legally permissible takes into account any legal restrictions on the use of the asset that market participants would take into account when pricing the asset (for example, the zoning regulations applicable to a property).

c. A use that is financially feasible takes into account whether a use of the asset that is physically possible and legally permissible generates adequate income or cash flows (taking into account the costs of converting the asset to that use) to produce an investment return that market participants would require from an investment in that asset put to that use.

Highest and best use is determined from the perspective of market participants, even if the reporting entity intends a different use. However, a reporting entity's current use of a nonfinancial asset is presumed to be its highest and best use unless market or other factors suggest that a different use by market participants would maximize the value of the asset.

To protect its competitive position, or for other reasons, a reporting entity may intend not to use an acquired nonfinancial asset actively, or it may intend not to use the asset according to its highest and best use. For example, that might be the case for an acquired intangible asset that the reporting entity plans to use defensively by preventing others from using it. Nevertheless, the reporting entity shall measure the fair value of a nonfinancial asset assuming its highest and best use by market participants.

Valuation Premise for Nonfinancial Assets

The highest and best use of a nonfinancial asset establishes the valuation premise used to measure the fair value of the asset, as follows:

a. The highest and best use of a nonfinancial asset might provide maximum value to market participants through its use in combination with other assets as a group (as installed or otherwise configured for use) or in combination with other assets and liabilities (for example, a business).

1. If the highest and best use of the asset is to use the asset in combination with other assets or with other assets and liabilities, the fair value of the asset is the price that would be received in a current transaction to sell the asset assuming that the asset would be used with other assets or with other assets and liabilities and that those assets and liabilities (that is, its complementary assets and the associated liabilities) would be available to market participants.

2. Liabilities associated with the asset and with the complementary assets include liabilities that fund working capital, but do not include liabilities used to fund assets other than those within the group of assets.

3. Assumptions about the highest and best use of a nonfinancial asset shall be consistent for all of the assets (for which highest and best use is relevant) of the group of assets or the group of assets and liabilities within which the asset would be used.

b. The highest and best use of a nonfinancial asset might provide maximum value to market participants on a standalone basis. If the highest and best use of the asset is to use it on a standalone basis, the fair value of the asset is the price that would be received in a current transaction to sell the asset to market participants that would use the asset on a standalone basis.

The fair value measurement of a nonfinancial asset assumes that the asset is sold consistent with the unit of account specified in other Topics (which may be an individual asset). That is the case even when that fair value measurement assumes that the highest and best use of the asset is to use it in combination with other assets or with other assets and liabilities because a fair value measurement assumes that the market participant already holds the complementary assets and associated liabilities.
ASC 820-10 (continued)

35-14 Paragraph 820-10-55-25 illustrates the application of the highest and best use and valuation premise concepts for nonfinancial assets.

An entity must measure the fair value of nonfinancial assets (other than nonfinancial derivative assets) on the basis of the appropriate valuation premise. The unit of valuation (also referred to as the “valuation premise”) for nonfinancial assets (other than nonfinancial derivative assets) is the asset’s highest and best use. See Chapter 5 for more information about the valuation premise for nonfinancial assets, including the illustrations in ASC 820-10-55.

10.2.7 Application to Liabilities and Instruments Classified in Equity

10.2.7.1 General

ASC 820-10

General Principles

35-16 A fair value measurement assumes that a financial or nonfinancial liability or an instrument classified in a reporting entity's shareholders’ equity (for example, equity interests issued as consideration in a business combination) is transferred to a market participant at the measurement date. The transfer of a liability or an instrument classified in a reporting entity's shareholders’ equity assumes the following: . . .

b. A liability would remain outstanding and the market participant transferee would be required to fulfill the obligation. The liability would not be settled with the counterparty or otherwise extinguished on the measurement date.

c. An instrument classified in a reporting entity's shareholders’ equity would remain outstanding and the market participant transferee would take on the rights and responsibilities associated with the instrument. The instrument would not be cancelled or otherwise extinguished on the measurement date.

35-16A Even when there is no observable market to provide pricing information about the transfer of a liability or an instrument classified in a reporting entity's shareholders’ equity (for example, because contractual or other legal restrictions prevent the transfer of such items), there might be an observable market for such items if they are held by other parties as assets (for example, a corporate bond or a call option on a reporting entity's shares).

35-16AA In all cases, a reporting entity shall maximize the use of relevant observable inputs and minimize the use of unobservable inputs to meet the objective of a fair value measurement, which is to estimate the price at which an orderly transaction to transfer the liability or instrument classified in shareholders’ equity would take place between market participants at the measurement date under current market conditions.

ASC 820-10-35-16 indicates that when a liability or instrument classified in an entity’s equity is measured at fair value, it is assumed that the instrument is transferred to a market participant as of the measurement date (i.e., the liability or equity instrument remains outstanding and is not extinguished or canceled). ASC 820-10-35-16A clarifies that this is the case even if (1) “there is no observable market to provide pricing information” regarding the transfer of a liability or equity-classified instrument or (2) there are “contractual or other legal restrictions” preventing a transfer. Further, in accordance with the general principles related to fair value measurements, ASC 820-10-35-16AA indicates that an entity should “maximize the use of relevant observable inputs and minimize the use of unobservable inputs.” An entity may estimate the fair value of a liability instrument or instrument classified in an entity’s equity on the basis of the fair value of the item when held by another party as an asset.
10.2.7.2 Liabilities and Instruments Classified in Equity That Are Held by Other Parties as Assets

<table>
<thead>
<tr>
<th>ASC 820-10</th>
</tr>
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</table>

**Liabilities and Instruments Classified in a Reporting Entity's Shareholders' Equity Held by Other Parties as Assets**

**35-16B** When a quoted price for the transfer of an identical or a similar liability or instrument classified in a reporting entity's shareholders' equity is not available and the identical item is held by another party as an asset, a reporting entity shall measure the fair value of the liability or equity instrument from the perspective of a market participant that holds the identical item as an asset at the measurement date.

**35-16BB** In such cases, a reporting entity shall measure the fair value of the liability or equity instrument as follows:

a. Using the quoted price in an active market for the identical item held by another party as an asset, if that price is available

b. If that price is not available, using other observable inputs, such as the quoted price in a market that is not active for the identical item held by another party as an asset

c. If the observable prices in (a) and (b) are not available, using another valuation approach, such as:
   1. An income approach (for example, a present value technique that takes into account the future cash flows that a market participant would expect to receive from holding the liability or equity instrument as an asset; see paragraph 820-10-55-3F)
   2. A market approach (for example, using quoted prices for similar liabilities or instruments classified in shareholders' equity held by other parties as assets; see paragraph 820-10-55-3A).

| **35-16D** |

A reporting entity shall adjust the quoted price of a liability or an instrument classified in a reporting entity's shareholders' equity held by another party as an asset only if there are factors specific to the asset that are not applicable to the fair value measurement of the liability or equity instrument. A reporting entity shall ensure that the price of the asset does not reflect the effect of a restriction preventing the sale of that asset. Some factors that may indicate that the quoted price of the asset should be adjusted include the following:

a. The quoted price for the asset relates to a similar (but not identical) liability or equity instrument held by another party as an asset. For example, the liability or equity instrument may have a particular characteristic (for example, the credit quality of the issuer) that is different from that reflected in the fair value of the similar liability or equity instrument held as an asset.

b. The unit of account for the asset is not the same as for the liability or equity instrument. For example, for liabilities, in some cases the price for an asset reflects a combined price for a package comprising both the amounts due from the issuer and a third-party credit enhancement. If the unit of account for the liability is not for the combined package, the objective is to measure the fair value of the issuer's liability, not the fair value of the combined package. Thus, in such cases, the reporting entity would adjust the observed price for the asset to exclude the effect of the third-party credit enhancement. See paragraph 820-10-35-18A for further guidance.
Quoted prices for the transfer of a liability or instrument classified in stockholders' equity are generally not available. Therefore, ASC 820-10-35-16B specifies that an entity should measure the fair value of liabilities and instruments classified in equity “from the perspective of a market participant that holds the identical item as an asset at the measurement date.” As with other measurements under ASC 820, the fair value of a liability or instrument classified in equity that is determined from the perspective of a market participant that holds the item as an asset should be measured by maximizing observable inputs and minimizing unobservable inputs. ASC 820-10-35-16BB provides the following hierarchy for such measurement:

1. Use “the quoted price in an active market for the identical item held by another party as an asset, if that price is available.” Otherwise, proceed to the next step.
2. Use “the quoted price in a market that is not active for the identical item held by another party as an asset,” if that price is available. Otherwise, proceed to the next step.
3. Use a valuation approach to measure the fair value of the identical item held by another party as an asset (i.e., an income or market approach).

An entity sometimes may need to adjust the quoted price of an asset to properly reflect factors that do not apply to the fair value of a liability or instrument classified in equity. As discussed in ASC 820-10-35-16D, the need for such an adjustment usually arises because either (1) the observed price is related to a similar, but not identical, asset that is used to measure the fair value of a liability or equity instrument or (2) the unit of account for the asset differs from the unit of account for the liability or equity instrument. ASC 820-10-35-16D also clarifies how restrictions preventing the sale of an asset should be considered when the quoted price of the asset is used to measure the fair value of a liability or equity instrument. See Section 10.2.7.4 for discussion of the incorporation of adjustments for risk and transferability restrictions into the measurement of the fair value of liability instruments. See Section 10.6 for discussion of situations in which the volume or level of activity for an asset or a liability has significantly decreased.

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10 As discussed in Section 4.3.2.2, the unit of account for a liability instrument that is measured at fair value excludes inseparable third-party credit enhancements in accordance with ASC 825-10-25-13. See also Section 10.2.7.3.
When any adjustment is made to a quoted price of an item held as an asset, the fair value measurement of the liability or equity instrument cannot be classified within Level 1 of the fair value hierarchy. Rather, the entity must evaluate the nature of any such adjustments to determine whether the fair value measurement in its entirety should be classified within Level 2 or 3 of the fair value hierarchy. See Chapter 8 for further discussion of the fair value hierarchy.

Case D of Example 7 in ASC 820 illustrates the measurement of the fair value of a liability on the basis of a quoted price of the identical item held by another party as an asset (see Section 10.2.7.5).

10.2.7.3 Liabilities and Instruments Classified in Equity That Are Not Held by Other Parties as Assets

**ASC 820-10**

**Liabilities and Instruments Classified in a Reporting Entity’s Shareholders’ Equity Not Held by other Parties as Assets**

35-16H When a quoted price for the transfer of an identical or a similar liability or instrument classified in a reporting entity’s shareholders’ equity is not available and the identical item is not held by another party as an asset, a reporting entity shall measure the fair value of the liability or equity instrument using a valuation technique from the perspective of a market participant that owes the liability or has issued the claim on equity.

35-16L For example, when applying a present value technique, a reporting entity might take into account either of the following:

   a. The future cash outflows that a market participant would expect to incur in fulfilling the obligation, including the compensation that a market participant would require for taking on the obligation (see paragraphs 820-10-35-16J through 35-16K).

   b. The amount that a market participant would receive to enter into or issue an identical liability or equity instrument, using the assumptions that market participants would use when pricing the identical item (for example, having the same credit characteristics) in the principal (or most advantageous) market for issuing a liability or an equity instrument with the same contractual terms.

35-16J When using a present value technique to measure the fair value of a liability that is not held by another party as an asset (for example, an asset retirement obligation), a reporting entity shall, among other things, estimate the future cash outflows that market participants would expect to incur in fulfilling the obligation. Those future cash outflows shall include market participants’ expectations about the costs of fulfilling the obligation and the compensation that a market participant would require for taking on the obligation. Such compensation includes the return that a market participant would require for the following:

   a. Undertaking the activity (that is, the value of fulfilling the obligation — for example, by using resources that could be used for other activities)

   b. Assuming the risk associated with the obligation (that is, a risk premium that reflects the risk that the actual cash outflows might differ from the expected cash outflows; see paragraph 820-10-35-16L).

35-16K For example, a nonfinancial liability does not contain a contractual rate of return and there is no observable market yield for that liability. In some cases, the components of the return that market participants would require will be indistinguishable from one another (for example, when using the price a third-party contractor would charge on a fixed-fee basis). In other cases, a reporting entity needs to estimate those components separately (for example, when using the price a third-party contractor would charge on a cost-plus basis because the contractor in that case would not bear the risk of future changes in costs).
35-16L A reporting entity can include a risk premium in the fair value measurement of a liability or an instrument classified in a reporting entity's shareholders' equity that is not held by another party as an asset in one of the following ways:

a. By adjusting the cash flows (that is, as an increase in the amount of cash outflows)
b. By adjusting the rate used to discount the future cash flows to their present values (that is, as a reduction in the discount rate).

A reporting entity shall ensure that it does not double count or omit adjustments for risk. For example, if the estimated cash flows are increased to take into account the compensation for assuming the risk associated with the obligation, the discount rate should not be adjusted to reflect that risk.

ASC 820-10-35-16H through 35-16L address how to measure the fair value of a liability or instrument classified in stockholders' equity when (1) “a quoted price for the transfer of an identical or [similar] instrument . . . is not available” and (2) “the identical item is not held by another party as an asset.” This guidance will generally apply only to nonfinancial liabilities because financial liabilities and instruments that an entity classifies in equity would be expected to be held by another party on an identical basis as an asset. However, an entity would not be precluded from estimating the fair value of a liability or equity instrument in accordance with ASC 820-10-35-16H through 35-16L so that it can calibrate the fair value measurement to the estimate in accordance with ASC 820-10-35-16BB(c).

As with other fair value measurements under ASC 820, a fair value measurement estimated in accordance with ASC 820-10-35-16H through 35-16L should maximize observable inputs and minimize unobservable inputs. Such measurement should also incorporate the entity's nonperformance risk and relevant risk premiums (see Section 10.2.7.4 for more information). A fair value measurement in accordance with ASC 820-10-35-16H through 35-16L can never be classified as a Level 1 measurement in its entirety.

Case C of Example 7 in ASC 820 illustrates the use of a valuation technique to estimate the fair value of an ARO liability (see Section 10.2.7.5).

10.2.7.4 Adjustments for Risk and Transferability Restrictions

10.2.7.4.1 General

Liabilities and Instruments Classified in a Reporting Entity's Shareholders' Equity Not Held by Other Parties as Assets

35-16J When using a present value technique to measure the fair value of a liability that is not held by another party as an asset (for example, an asset retirement obligation), a reporting entity shall, among other things, estimate the future cash outflows that market participants would expect to incur in fulfilling the obligation. Those future cash outflows shall include market participants' expectations about the costs of fulfilling the obligation and the compensation that a market participant would require for taking on the obligation. Such compensation includes the return that a market participant would require for the following:

a. Undertaking the activity (that is, the value of fulfilling the obligation — for example, by using resources that could be used for other activities)
b. Assuming the risk associated with the obligation (that is, a risk premium that reflects the risk that the actual cash outflows might differ from the expected cash outflows; see paragraph 820-10-35-16L).
A reporting entity can include a risk premium in the fair value measurement of a liability or an instrument classified in a reporting entity's shareholders' equity that is not held by another party as an asset in one of the following ways:

a. By adjusting the cash flows (that is, as an increase in the amount of cash outflows)

b. By adjusting the rate used to discount the future cash flows to their present values (that is, as a reduction in the discount rate).

A reporting entity shall ensure that it does not double count or omit adjustments for risk. For example, if the estimated cash flows are increased to take into account the compensation for assuming the risk associated with the obligation, the discount rate should not be adjusted to reflect that risk.

Nonperformance Risk

The fair value of a liability reflects the effect of nonperformance risk. Nonperformance risk includes, but may not be limited to, a reporting entity's own credit risk. Nonperformance risk is assumed to be the same before and after the transfer of the liability.

When measuring the fair value of a liability, a reporting entity shall take into account the effect of its credit risk (credit standing) and any other factors that might influence the likelihood that the obligation will or will not be fulfilled. That effect may differ depending on the liability, for example:

a. Whether the liability is an obligation to deliver cash (a financial liability) or an obligation to deliver goods or services (a nonfinancial liability)

b. The terms of credit enhancements related to the liability, if any.

Paragraph 820-10-55-56 illustrates the effect of credit risk on the fair value measurement of a liability.

The fair value of a liability reflects the effect of nonperformance risk on the basis of its unit of account. In accordance with Topic 825, the issuer of a liability issued with an inseparable third-party credit enhancement that is accounted for separately from the liability shall not include the effect of the credit enhancement (for example, a third-party guarantee of debt) in the fair value measurement of the liability. If the credit enhancement is accounted for separately from the liability, the issuer would take into account its own credit standing and not that of the third-party guarantor when measuring the fair value of the liability.

Restriction Preventing the Transfer of a Liability or an Instrument Classified in a Reporting Entity's Shareholders' Equity

When measuring the fair value of a liability or an instrument classified in a reporting entity's shareholders' equity, a reporting entity shall not include a separate input or an adjustment to other inputs relating to the existence of a restriction that prevents the transfer of the item. The effect of a restriction that prevents the transfer of a liability or an instrument classified in a reporting entity's shareholders' equity is either implicitly or explicitly included in the other inputs to the fair value measurement.

For example, at the transaction date, both the creditor and the obligor accepted the transaction price for the liability with full knowledge that the obligation includes a restriction that prevents its transfer. As a result of the restriction being included in the transaction price, a separate input or an adjustment to an existing input is not required at the transaction date to reflect the effect of the restriction on transfer. Similarly, a separate input or an adjustment to an existing input is not required at subsequent measurement dates to reflect the effect of the restriction on transfer.
Credit Risk
For purposes of a hedged item in a fair value hedge, credit risk is the risk of changes in the hedged item's fair value attributable to both of the following:
  a. Changes in the obligor's creditworthiness
  b. Changes in the spread over the benchmark interest rate with respect to the hedged item's credit sector at inception of the hedge.

For purposes of a hedged transaction in a cash flow hedge, credit risk is the risk of changes in the hedged transaction's cash flows attributable to all of the following:
  a. Default
  b. Changes in the obligor's creditworthiness
  c. Changes in the spread over the benchmark interest rate with respect to the related financial asset's or liability's credit sector at inception of the hedge.

Note: The following definition is Pending Content; see Transition Guidance in 815-20-65-3.

Nonperformance Risk
The risk that an entity will not fulfill an obligation. Nonperformance risk includes, but may not be limited to, the reporting entity's own credit risk.

Risk Premium
Compensation sought by risk-averse market participants for bearing the uncertainty inherent in the cash flows of an asset or a liability. Also referred to as a risk adjustment.

A liability or equity-classified instrument may be subject to various risks, including instrument-specific (e.g., issuer-specific), industry-specific, and market risks (e.g., risks related to general economic conditions). ASC 820-10-35-16 through 35-18C address the incorporation of risk adjustments into the fair value of a liability or an instrument classified in stockholders' equity. According to that guidance:

- A risk premium should be incorporated into the fair value measurement of a liability to the extent that market participants would demand a premium as compensation for assuming the risk of uncertain cash flows. Risk premiums are also relevant to fair value measurements of instruments classified in stockholders' equity.

- The fair value of a liability takes into account the impact of nonperformance risk, including, but not limited to, credit risk. Nonperformance risk could also be relevant to fair value measurements of instruments classified in stockholders' equity if those equity instruments are redeemable.
In determining fair value, an entity should not make an adjustment for the nontransferability of a liability instrument or instrument classified in stockholders' equity (see further clarification in Section 10.2.7.4.4).

While the above guidance from ASC 820 addresses fair value measurements performed on the basis of a present value technique used to measure the fair value of a liability instrument or instrument classified in stockholders' equity when such an instrument is not held by another entity as an asset, the same concepts apply when the liability instrument or instrument classified in stockholders' equity is measured on the basis of the identical item held by another entity as an asset. However, in the latter case, the relevant adjustments for nonperformance risk, risk premiums, and transferability restrictions will be reflected explicitly or implicitly in the fair value measurement of the related asset.

### 10.2.7.4.2 Risk Premiums

The cash flows associated with certain liability instruments and instruments classified in stockholders' equity (and the corresponding items held as an asset by another entity, if applicable) are uncertain (i.e., there are risks related to either the amount or timing of cash flows). In these situations, the fair value measurement of the liability must incorporate an adjustment that reflects a risk premium on the basis of market-participant assumptions (i.e., the compensation market participants would demand for bearing such risks). Note that risk premiums are intended to reflect premiums for compensation related to bearing the risk of the instrument's uncertain cash flows that arise because the cash flows are indexed to an underlying other than nonperformance risk (e.g., a liability whose principal and interest are indexed to the price of gold). The premium demanded by a market participant to bear nonperformance risk is reflected by adjusting a fair value measurement to take such risk into account. To reflect that premium as both a risk premium and a premium for nonperformance risk would be inappropriate since it would double-count the risk's impact.

ASC 820-10-35-16L indicates that a risk premium may be incorporated into a discounted cash flow technique by (1) adjusting the cash flows (i.e., the use of probability-weighted cash flows), (2) adjusting the rate used to discount cash flows, or (3) aspects of both. However, an entity is not permitted to double-count or omit such risk adjustments. Such risk adjustments would be incorporated, as necessary, regardless of whether the fair value of a liability or instrument classified in stockholders' equity is measured by using a present value technique under ASC 820-10-35-16BB(c) (i.e., to measure the fair value of the corresponding identical item held by another party as an asset) or ASC 820-10-35-16H through 35-16L (i.e., to measure the fair value of the liability because it is not held as an asset by another party). A separate adjustment for a risk premium is unnecessary when the fair value of a liability or instrument classified in stockholders' equity is measured on the basis of a quoted price for the identical item held by another party as an asset, since the quoted price will already reflect compensation for such risk. If the fair value of a liability or instrument classified in stockholders' equity is measured on the basis of a quoted price for a similar, but not identical, item held by another party as an asset, an adjustment for a risk premium would also be unnecessary unless the difference arises because of uncertain cash flows.

Case C of Example 7 in ASC 820 illustrates the impact that a market risk premium may have on the fair value of an ARO liability (see Section 10.2.7.5).
10.2.7.4.3 Nonperformance Risk

The ASC master glossary defines nonperformance risk as “the risk that an entity will not fulfill an obligation.” Nonperformance risk includes, but is a broader concept than, credit risk, which is the risk that an entity will not make payments of cash or other financial instruments in accordance with the terms of an obligation.

Nonperformance risk is associated with all liabilities. For some liabilities (i.e., financial liabilities), nonperformance risk consists entirely of the credit risk of the obligor (e.g., a financial liability that requires the obligor to make contractual principal and interest payments). Other liabilities (i.e., nonfinancial liabilities) pose nonperformance risks for reasons other than credit risk. In addition to an entity's own credit risk, nonperformance risk might include the risk associated with the entity's ability to deliver a good or perform a service. Consider a derivative liability associated with a contract for the delivery of a commodity (e.g., oil, natural gas, electricity) that is carried at fair value. Nonperformance risk would include the risk that the entity will not be able to obtain and deliver the commodity to the counterparty.

ASC 820-10-35-17 and 35-18 and ASC 820-10-55-56 indicate that the fair value of a liability must reflect the nonperformance risk of the instrument. For example, an entity must take into account the effect of credit risk (credit standing) on the fair value of a financial liability in all periods in which the liability is measured at fair value because other entities would take into account the effect of the entity's credit risk when estimating the price they would be willing to pay to own the instrument as an asset. Entities should consider nonperformance risk when measuring both financial and nonfinancial liabilities at fair value. ASC 820-10-35-16 states, in part, that “[a] fair value measurement assumes that a financial or nonfinancial liability . . . is transferred to a market participant [that assumes the obligation] at the measurement date.” ASC 820-10-35-17 adds that “[n]onperformance risk is assumed to be the same before and after the transfer of the liability.” Thus, under ASC 820, it is assumed that the transferor's credit risk is similar to that of the transferee. Accordingly, to the extent that the fair value of a liability is not determined on the basis of the fair value of the identical item owned as an asset by another party, the entity must ensure that adjustments for nonperformance risk do not result in a change in the nonperformance risk for the liability.

The extent to which nonperformance risk affects the fair value of a liability depends on various factors, including the unit of account for the liability, credit spreads, entity-specific credit standing, and credit enhancements. Collateral is a form of credit enhancement that is contractually linked to an obligation (i.e., the provisions of the obligation require a lien on the collateral until the obligation is settled). It typically affects the stated terms of liabilities (e.g., the interest rate charged to a borrower). Thus, in estimating the fair value of a collateralized liability, an entity should assume that the lender would require the borrower, to whom the obligation would be transferred, to post the amount of collateral that is stipulated in that particular arrangement. However, the unit of account for a liability excludes an inseparable third-party credit enhancement that is accounted for separately from the liability. Therefore, the fair value of such liabilities should not take into account the third-party credit enhancement. Rather, an entity measures the fair value of such liabilities under the assumption that the third-party credit enhancement did not exist (i.e., the issuer would take into account its own credit standing and not that of the third-party guarantor when measuring the fair value of the liability). See Section 12.3.1.1.1.1 for further discussion of when third-party credit enhancements are treated as a separate unit of account. See Section 10.2.7.2 for discussion of the need to make adjustments to the quoted price of an asset that includes the impact of a third-party credit enhancement when the fair value of a liability is measured on the basis of the identical item held by another party as an asset.
Nonperformance risks related to nonfinancial liabilities, such as commodity delivery contracts or service contracts may be mitigated by “make-whole” or other default provisions that require an entity to make cash payments for damages incurred if it fails to meet its delivery or service obligation. However, the entity must still consider credit risk since it may be unable to meet such cash payment obligations.

**Connecting the Dots**

As discussed in Section 10.1, the best practices and guidance in the IASB’s Expert Advisory Panel report are useful to entities that measure and disclose the fair values of financial instruments in accordance with ASC 820. Paragraph 35 of the report addresses factors an entity may consider in evaluating the credit risk of a debt instrument and states the following:

Understanding the credit risk of a debt instrument involves evaluating the credit quality and financial strength of both the issuer and the credit support providers. There are many factors an entity might consider and some of the more common factors are as follows:

(a) **collateral asset quality**: the assets to which the holder of an instrument has recourse in the event of non-payment or default could be either all of the assets of the issuing entity or specified assets that are legally separated from the issuer (ring-fenced). The greater the value and quality of the assets to which an entity has recourse in the event of default, the lower the credit risk of the instrument. Measuring the fair value of a debt instrument therefore involves assessing the quality of the assets that support the instrument (the collateral) and the level of the collateralisation, and evaluating the likelihood that the assigned collateral will generate adequate cash flows to make the contractual payments on the instrument.

(b) **subordination**: the level of subordination of an instrument is critical to assessing the risk of non-payment of an instrument. If other more senior instruments have higher claims over the cash flows and assets that support the instrument, this increases the risk of the instrument. The lower the claim on the cash flows and assets, the more risky an instrument is and the higher the return the market will demand on the instrument.

(c) **non-payment protection**: many instruments contain some form of protection to reduce the risk of non-payment to the holder. In measuring fair value, both the issuer and the holder of the instrument consider the effect of the protection on the fair value of the instrument, unless the entity accounts for the protection as a separate instrument. Protection might take the form of a guarantee or a similar undertaking (e.g., when a parent guarantees the debt of a subsidiary), an insurance contract, a credit default swap or simply the fact that more assets support the instrument than are needed to make the payments (this is commonly referred to as over-collateralisation). The risk of non-payment is also reduced by the existence of more subordinated tranches of instruments that take the first losses on the underlying assets and therefore reduce the risk of more senior tranches absorbing losses. When protection is in the form of a guarantee, an insurance contract or a credit default swap (and that protection is not accounted for as a separate instrument), it is necessary to identify the party providing the protection and assess that party’s creditworthiness (to the extent that the protection is not accounted for separately). The protection will be more valuable if the credit risk of the protection provider is low. This analysis involves considering not only the current position of the protection provider but also the effect of other guarantees or insurance contracts that it might have written. For example, if the provider has guaranteed many correlated debt securities, the risk of its non-performance might increase significantly with increases in defaults on those securities. In addition, the credit risk of some protection providers moves as market conditions change. Thus, an entity evaluates the credit risk of each protection provider at each measurement date.

Although the above guidance is relevant to evaluating the nonperformance risk associated with an asset or liability, this evaluation is complex. Accordingly, an entity should consider engaging those with specialized knowledge (e.g., valuation experts, credit risk management specialists) to perform this analysis.
Cases A, B, C, and E of Example 7 in ASC 820 and Examples 10-10 through 10-12 in Section 10.2.7.5 illustrate the impact that nonperformance risk may have on the fair value measurement of liabilities.

10.2.7.4.3.1 Debt Assumed in a Business Combination

ASC 805-20-30-1 requires an acquirer to initially measure an acquiree's debt that is assumed in a business combination at fair value. If the acquirer guarantees the acquiree's debt, the credit characteristics of the combined entity should be considered when the fair value of the assumed debt obligation is initially measured. (This guidance is consistent with the discussion in EITF Issue 98-1.11) However, if the debt remains solely the acquiree's obligation (i.e., the acquirer does not guarantee or collateralize the debt), only the acquiree's credit risk should be considered as of the measurement date used to measure the fair value of the assumed debt.

10.2.7.4.4 Transferability Restrictions

Under ASC 820-10-35-18B, the fair value measurement of a liability instrument or instrument classified in stockholders' equity should not include a separate input or adjustment related to a contractual restriction that prevents the entity from transferring the item. ASC 820-10-35-18B states, in part, that “[t]he effect of a restriction that prevents the transfer of a liability or an instrument classified in a reporting entity’s shareholders’ equity is either implicitly or explicitly included in the other inputs to the fair value measurement.”

The fair value measurement of a liability instrument or instrument classified in stockholders' equity will often be determined on the basis of the fair value of the identical item held as an asset by another entity. In these circumstances, if there is a restriction on the transferability of the asset that is instrument-specific (as opposed to entity-specific), the fair value measurement of the asset will be affected by the restriction. In this circumstance, the fair value measurement of a liability instrument or instrument classified in stockholders' equity would similarly be affected by the restriction (i.e., the fair value measurement of the liability or equity instrument would not be adjusted to remove the impact of the restriction on the fair value of the identical item held by another party as an asset because the restriction does not represent a factor specific to the asset in accordance with ASC 820-10-35-16D). In summary, a restriction that prevents the holder of an asset from transferring, or affects its ability to transfer, this asset — when this restriction is appropriately incorporated into the fair value measurement of the asset — will also be incorporated into the fair value measurement of the liability or equity instrument from the perspective of the entity that has issued the liability or equity instrument. However, neither of the following transferability restrictions should have any impact on the fair value of a liability or equity instrument:

- A restriction on the transferability of an asset that is entity-specific.
- A restriction only on the issuer's ability to transfer its liability or own equity instruments.

See Section 10.2.2.2 for further discussion of how transfer restrictions affect fair value measurements of assets.

11 Although this EITF Issue was not codified, the concepts in it are consistent with the market-participant approach in ASC 820.
10.2.7.5 Examples

Example 7 in ASC 820 consists of several cases illustrating the fair value measurement of liabilities.

**ASC 820-10**

**Example 7: Measuring Liabilities**

55-55A A fair value measurement of a liability assumes that the liability, whether it is a financial liability or a nonfinancial liability, is transferred to a market participant at the measurement date (that is, the liability would remain outstanding and the market participant transferee would be required to fulfill the obligation; it would not be settled with the counterparty or otherwise extinguished on the measurement date).

55-56 The fair value of a liability reflects the effect of nonperformance risk. Nonperformance risk relating to a liability includes, but may not be limited to, the reporting entity’s own credit risk. A reporting entity takes into account the effect of its credit risk (credit standing) on the fair value of the liability in all periods in which the liability is measured at fair value because those that hold the reporting entity’s obligations as assets would take into account the effect of the reporting entity’s credit standing when estimating the prices they would be willing to pay. Cases A–E illustrate the measurement of liabilities and the effect of nonperformance risk (including a reporting entity’s own credit risk) on a fair value measurement.

**Case A: Liabilities and Credit Risk — General**

55-57 This Case has the following assumptions:

a. Entity X and Entity Y each enter into a contractual obligation to pay cash ($500) to Entity Z in 5 years.

b. Entity X has a AA credit rating and can borrow at 6 percent, and Entity Y has a BBB credit rating and can borrow at 12 percent

55-57A Entity X will receive about $374 in exchange for its promise (the present value of $500 in 5 years at 6 percent). Entity Y will receive about $284 in exchange for its promise (the present value of $500 in 5 years at 12 percent). The fair value of the liability to each entity (that is, the proceeds) incorporates that reporting entity’s credit standing.

**Case B: Structured Note**

55-59 On January 1, 20X7, Entity A, an investment bank with a AA credit rating, issues a five-year fixed rate note to Entity B. The contractual principal amount to be paid by Entity A at maturity is linked to the Standard and Poor's S&P 500 index. No credit enhancements are issued in conjunction with or otherwise related to the contract (that is, no collateral is posted and there is no third-party guarantee). Entity A elects to account for the entire note at fair value in accordance with paragraph 815-15-25-4. The fair value of the note (that is, the obligation of Entity A) during 20X7 is measured using an expected present value technique. Changes in fair value are as follows:

a. Fair value at January 1, 20X7. The expected cash flows used in the expected present value technique are discounted at the risk-free rate using the treasury yield curve at January 1, 20X7, plus the current market observable AA corporate bond spread to treasuries, if nonperformance risk is not already reflected in the cash flows, adjusted (either up or down) for Entity A's specific credit risk (that is, resulting in a credit-adjusted risk-free rate). Therefore, the fair value of Entity A’s obligation at initial recognition takes into account nonperformance risk, including that reporting entity's credit risk, which presumably is reflected in the proceeds.

b. Fair value at March 31, 20X7. During March 20X7, the credit spread for AA corporate bonds widens, with no changes to the specific credit risk of Entity A. The expected cash flows used in the expected present value technique are discounted at the risk-free rate using the treasury yield curve at March 31, 20X7, plus the current market observable AA corporate bond spread to treasuries if nonperformance risk is not already reflected in the cash flows, adjusted for Entity A's specific credit risk (that is, resulting in a credit-adjusted risk-free rate). Entity A's specific credit risk is unchanged from initial recognition. Therefore, the fair value of Entity A's obligation changes as a result of changes in credit spreads generally. Changes in credit spreads reflect current market participant assumptions about changes in nonperformance risk generally, changes in liquidity risk, and the compensation required for assuming those risks.
c. Fair value at June 30, 20X7. As of June 30, 20X7, there have been no changes to the AA corporate bond spreads. However, on the basis of structured note issues corroborated with other qualitative information, Entity A determines that its own specific creditworthiness has strengthened within the AA credit spread. The expected cash flows used in the expected present value technique are discounted at the risk-free rate using the treasury yield curve at June 30, 20X7, plus the current market observable AA corporate bond spread to treasuries (unchanged from March 31, 20X7), if nonperformance risk is not already reflected in the cash flows, adjusted for Entity A’s specific credit risk (that is, resulting in a credit-adjusted risk-free rate). Therefore, the fair value of the obligation of Entity A changes as a result of the change in its own specific credit risk within the AA corporate bond spread.

Case C: Asset Retirement Obligation

55-77 On January 1, 20X1, Entity A assumes an asset retirement obligation in a business combination. The reporting entity is legally required to dismantle and remove an offshore oil platform at the end of its useful life, which is estimated to be 10 years.

55-78 On the basis of paragraph 410-20-30-1, Entity A uses the expected present value technique to measure the fair value of the asset retirement obligation.

55-79 If Entity A was contractually allowed to transfer its asset retirement obligation to a market participant, Entity A concludes that a market participant would use all of the following inputs, probability-weighted as appropriate, when estimating the price it would expect to receive:

a. Labor costs
b. Allocation of overhead costs
c. The compensation that a market participant would require for undertaking the activity and for assuming the risk associated with the obligation to dismantle and remove the asset. Such compensation includes both of the following:
   1. Profit on labor and overhead costs
   2. The risk that the actual cash outflows might differ from those expected, excluding inflation.
d. Effect of inflation on estimated costs and profits
e. Time value of money, represented by the risk-free rate
f. Nonperformance risk relating to the risk that Entity A will not fulfill the obligation, including Entity A’s own credit risk.

55-80 The significant assumptions used by Entity A to measure fair value are as follows:

a. Labor costs are developed on the basis of current marketplace wages, adjusted for expectations of future wage increases, required to hire contractors to dismantle and remove offshore oil platforms. Entity A assigns probability assessments to a range of cash flow estimates as follows.

<table>
<thead>
<tr>
<th>Cash Flow Estimate</th>
<th>Probability Assessment</th>
<th>Expected Cash Flows</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ 100,000</td>
<td>25%</td>
<td>$ 25,000</td>
</tr>
<tr>
<td>125,000</td>
<td>50%</td>
<td>62,500</td>
</tr>
<tr>
<td>175,000</td>
<td>25%</td>
<td>43,750</td>
</tr>
<tr>
<td></td>
<td></td>
<td>$ 131,250</td>
</tr>
</tbody>
</table>
The probability assessments are developed on the basis of Entity A's experience with fulfilling obligations of this type and its knowledge of the market.

b. Entity A estimates allocated overhead and equipment operating costs using the rate it applies to labor costs (80 percent of expected labor costs). This is consistent with the cost structure of market participants.

c. Entity A estimates the compensation that a market participant would require for undertaking the activity and for assuming the risk associated with the obligation to dismantle and remove the asset as follows:

1. A third-party contractor typically adds a markup on labor and allocated internal costs to provide a profit margin on the job. The profit margin used (20 percent) represents Entity A's understanding of the operating profit that contractors in the industry generally earn to dismantle and remove offshore oil platforms. Entity A concludes that this rate is consistent with the rate that a market participant would require as compensation for undertaking the activity.

2. A contractor would typically require compensation for the risk that the actual cash outflows might differ from those expected because of the uncertainty inherent in locking in today's price for a project that will not occur for 10 years. Entity A estimates the amount of that premium to be 5 percent of the expected cash flows, including the effect of inflation.

d. Entity A assumes a rate of inflation of 4 percent over the 10-year period on the basis of available market data.

e. The risk-free rate of interest for a 10-year maturity on January 1, 20X1, is 5 percent. Entity A adjusts that rate by 3.5 percent to reflect its risk of nonperformance (that is, the risk that it will not fulfill the obligation), including its credit risk. Therefore, the discount rate used to compute the present value of the cash flows is 8.5 percent.

Entity A concludes that its assumptions would be used by market participants. In addition, Entity A does not adjust its fair value measurement for the existence of a restriction preventing it from transferring the liability. As illustrated in the following table, Entity A measures the fair value of its liability for the asset retirement obligation as $194,879.

<table>
<thead>
<tr>
<th>Expected Cash Flows 1/1/X1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expected labor costs</td>
</tr>
<tr>
<td>Allocated overhead and equipment costs (.80 × $131,250)</td>
</tr>
<tr>
<td>Contractor's profit markup [.20 × ($131,250 + 105,000)]</td>
</tr>
<tr>
<td>Expected cash flows before inflation adjustment</td>
</tr>
<tr>
<td>Inflation factor (4% for 10 years)</td>
</tr>
<tr>
<td>Expected cash flows adjusted for inflation</td>
</tr>
<tr>
<td>Market risk premium (.05 × $419,637)</td>
</tr>
<tr>
<td>Expected cash flows adjusted for market risk</td>
</tr>
<tr>
<td>Expected present value using discount rate of 8.5% for 10 years</td>
</tr>
</tbody>
</table>

Case D: Debt Obligation — Quoted Price

On January 1, 20X1, Entity B issues at par a $2 million BBB-rated exchange-traded 5-year fixed-rate debt instrument with an annual 10 percent coupon. Entity B has elected to account for this instrument using the fair value option.
On December 31, 20X1, the instrument is trading as an asset in an active market at $929 per $1,000 of par value after payment of accrued interest. Entity B uses the quoted price of the asset in an active market as its initial input into the fair value measurement of its liability ($929 × [$2 million ÷ $1,000] = $1,858,000).

In determining whether the quoted price of the asset in an active market represents the fair value of the liability, Entity B evaluates whether the quoted price of the asset includes the effect of factors not applicable to the fair value measurement of a liability, for example, whether the quoted price of the asset includes the effect of a third-party credit enhancement that would be separately accounted for from the perspective of the issuer. Entity B determines that no adjustments are required to the quoted price of the asset. Accordingly, Entity B concludes that the fair value of its debt instrument at December 31, 20X1, is $1,858,000. Entity B categorizes and discloses the fair value measurement of its debt instrument within Level 1 of the fair value hierarchy.

Case E: Debt Obligation — Present Value Technique

On January 1, 20X1, Entity C issues at par in a private placement a $2 million BBB-rated 5-year fixed-rate debt instrument with an annual 10 percent coupon. Entity C has elected to account for this instrument using the fair value option.

At December 31, 20X1, Entity C still carries a BBB credit rating. Market conditions, including available interest rates, credit spreads for a BBB-quality credit rating and liquidity, remain unchanged from the date the debt instrument was issued. However, Entity C’s credit spread has deteriorated by 50 basis points because of a change in its risk of nonperformance. After taking into account all market conditions, Entity C concludes that if it was to issue the instrument at the measurement date, the instrument would bear a rate of interest of 10.5 percent or Entity C would receive less than par in proceeds from the issue of the instrument.

For the purpose of this example, the fair value of Entity C’s liability is calculated using a present value technique. Entity C concludes that a market participant would use all of the following inputs (consistent with paragraph 820-10-55-5) when estimating the price the market participant would expect to receive to assume Entity C’s obligation:

- The terms of the debt instrument, including all of the following:
  1. Coupon rate of 10 percent
  2. Principal amount of $2 million
  3. Term of 4 years.
- The market rate of interest of 10.5 percent (which includes a change of 50 basis points in the risk of nonperformance from the date of issue).

On the basis of its present value technique, Entity C concludes that the fair value of its liability at December 31, 20X1, is $1,968,641.

Entity C does not include any additional input into its present value technique for risk or profit that a market participant might require for compensation for assuming the liability. Because Entity C’s obligation is a financial liability, Entity C concludes that the interest rate already captures the risk or profit that a market participant would require as compensation for assuming the liability. Furthermore, Entity C does not adjust its present value technique for the existence of a restriction preventing it from transferring the liability.
Below are some additional examples illustrating the impact of collateral on the fair value measurements of liabilities.

### Example 10-10

**How Collateral Affects Fair Value of Liabilities**

Entity J has unsecured obligations. If these obligations were rated by a nationally recognized credit agency, a below-investment-grade rating (e.g., BB) would be warranted. On January 1, 20X3, J borrows $10 million in exchange for a fixed-rate, five-year bullet maturity debt at a 125-basis-point spread over the prevailing interest rate on five-year U.S. Treasury bonds (for simplicity, transaction costs are ignored). The lender requires J to collateralize its obligation by granting a security interest in designated machinery and equipment. Management estimates that J could have arranged a similar loan with no collateral at a 200-basis-point spread to five-year U.S. Treasury bonds. On January 1, 20X3, five-year U.S. Treasury bonds yielded 7 percent.

As of January 1, 20X3, the fair value of the loan (including any impact from the collateral) is $10 million. The present value of the loan's contractual cash flows, discounted at J's unsecured borrowing rate of 9 percent (7 percent plus 200 basis points), is $9.7 million. This example illustrates that both an issuer's credit standing and the effect of credit enhancements must be considered in the determination of the fair value of the liability. If J ignored the reduction in the interest rate attributable to the effect of collateral, it would have mistakenly concluded that the fair value of its debt was $9.7 million rather than $10 million.

**Impact of Collateral and Other Factors on the Fair Value of a Liability**

In subsequent periods, J should consider factors that affect the fair value of the obligation, including the following:

- Current levels of the benchmark interest rate.
- Credit spreads on comparable, collateralized obligations.
- Other terms of the obligation (e.g., put or call rights).
- Other current, relevant market information (e.g., regulatory considerations).
- The collateral’s current fair value.

Note that, in this example, the liability would be held as an identical asset by another party. The fair value measurement of such an asset would not differ from that in the discussion above.

### Example 10-11

**Effect of a Decline in Collateral’s Fair Value on a Collateralized Debt Instrument**

On January 1, 20X3, Entity K issues $100 million of notes collateralized by a portion of its aircraft fleet. As of September 30, 20X3, there has been a substantial decline in the fair value of the aircraft that serves as collateral for the notes. Assume that K’s credit standing remains unchanged and that all other stated terms of the notes represent current market conditions for the remaining term of the obligation (e.g., benchmark rate or spread over benchmark rates).

In determining the fair value of the obligation, K will have to consider the decline in the fair value of the collateral. While considering this effect, K determines that the fair value of the identical item held as an asset by another party would only represent a payment of $80 million for the asset and therefore that no adjustments are necessary under ASC 820-10-35-16D. Thus, the fair value of the notes has decreased by $20 million even though K’s credit standing remains unchanged.

### Example 10-12

**Effect of a Decline in the Borrower’s Credit Standing on a Collateralized Obligation**

Assume the same facts as in Example 10-11 except that the fair value of the aircraft has not changed; instead, the credit standing of K has declined. In determining the fair value of the obligation, K will have to consider the effect of the decline in its credit standing. Entity K will also need to consider the fact that the fair value of the collateral has not changed.
10.2.8 Application to Financial Assets and Financial Liabilities With Offsetting Risk Positions

10.2.8.1 General

ASC 820-10

Application to Financial Assets and Financial Liabilities With Offsetting Positions in Market Risks or Counterparty Credit Risk

35-18D A reporting entity that holds a group of financial assets and financial liabilities is exposed to market risks (that is, interest rate risk, currency risk, or other price risk) and to the credit risk of each of the counterparties. If the reporting entity manages that group of financial assets and financial liabilities on the basis of its net exposure to either market risks or credit risk, the reporting entity is permitted to apply an exception to this Topic for measuring fair value. That exception permits a reporting entity to measure the fair value of a group of financial assets and financial liabilities on the basis of the price that would be received to sell a net long position (that is, an asset) for a particular risk exposure or paid to transfer a net short position (that is, a liability) for a particular risk exposure in an orderly transaction between market participants at the measurement date under current market conditions. Accordingly, a reporting entity shall measure the fair value of the group of financial assets and financial liabilities consistently with how market participants would price the net risk exposure at the measurement date.

Pending Content (Transition Guidance: ASC 105-10-65-5)

35-18D A reporting entity that holds a group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items is exposed to market risks (that is, interest rate risk, currency risk, or other price risk) and to the credit risk of each of the counterparties. If the reporting entity manages that group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items on the basis of its net exposure to either market risks or credit risk, the reporting entity is permitted to apply an exception to this Topic for measuring fair value. That exception permits a reporting entity to measure the fair value of a group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items on the basis of the price that would be received to sell a net long position (that is, an asset) for a particular risk exposure or paid to transfer a net short position (that is, a liability) for a particular risk exposure in an orderly transaction between market participants at the measurement date under current market conditions. Accordingly, a reporting entity shall measure the fair value of the group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items consistently with how market participants would price the net risk exposure at the measurement date.

35-18E A reporting entity is permitted to use the exception in the preceding paragraph only if the reporting entity does all of the following:

a. Manages the group of financial assets and financial liabilities on the basis of the reporting entity’s net exposure to a particular market risk (or risks) or to the credit risk of a particular counterparty in accordance with the reporting entity’s documented risk management or investment strategy
b. Provides information on that basis about the group of financial assets and financial liabilities to the reporting entity’s management
c. Is required or has elected to measure those financial assets and financial liabilities at fair value in the statement of financial position at the end of each reporting period.
A reporting entity is permitted to use the exception in paragraph 820-10-35-18D only if the reporting entity does all of the following:

a. Manages the group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items on the basis of the reporting entity's net exposure to a particular market risk (or risks) or to the credit risk of a particular counterparty in accordance with the reporting entity's documented risk management or investment strategy

b. Provides information on that basis about the group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items to the reporting entity's management

c. Is required or has elected to measure those financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items at fair value in the statement of financial position at the end of each reporting period.

The exception in paragraph 820-10-35-18D does not pertain to financial statement presentation. In some cases, the basis for the presentation of financial instruments in the statement of financial position differs from the basis for the measurement of financial instruments, for example, if a Topic does not require or permit financial instruments to be presented on a net basis. In such cases, a reporting entity may need to allocate the portfolio-level adjustments (see paragraphs 820-10-35-18I through 35-18L) to the individual assets or liabilities that make up the group of financial assets and financial liabilities managed on the basis of the reporting entity's net risk exposure. A reporting entity shall perform such allocations on a reasonable and consistent basis using a methodology appropriate in the circumstances.
As discussed in Section 4.3.2, the unit of valuation for financial assets, nonfinancial derivative assets, all liabilities, and equity instruments is generally the individual instrument, which is generally also its unit of account under other GAAP. An exception to this general principle is available for groups of financial assets and financial liabilities if an entity (1) manages the group of assets and liabilities on the basis of net exposure to a market risk (or risks) or counterparty credit risk, (2) provides information on that basis to management, and (3) measures those assets and liabilities at fair value in the statement of financial position. ASC 820-10-35-18D indicates that an entity that uses this exception is permitted “to measure the fair value of a group of financial assets and financial liabilities on the basis of the price that would be received to sell a net long position (that is, an asset) for a particular risk exposure or paid to transfer a net short position (that is, a liability) for a particular risk exposure in an orderly transaction between market participants at the measurement date under current market conditions.” Accordingly, an entity that elects this exception should “measure the fair value of the group of financial assets and financial liabilities consistently with how market participants would price the net risk exposure at the measurement date.” This valuation exception may only be applied to a portfolio that includes eligible assets and eligible liabilities.

This exception applies only to valuation. It does not apply to financial statement presentation or disclosures required under other GAAP; thus, entities that apply this exception will be required to allocate the portfolio-level adjustments to the individual assets and liabilities that make up the portfolio managed on the basis of a net risk exposure. ASC 820 does not prescribe how an entity should allocate such portfolio adjustments but requires that any allocation approach be reasonable and consistently applied. See Section 11.2.3.5.5 for further discussion.

An entity must make an accounting policy decision to use the portfolio valuation exception. Once the policy is established for a particular portfolio, the entity must consistently apply that policy to the portfolio and must consistently apply its policy for allocating bid-ask adjustments and credit adjustments to the individual eligible items within the portfolio. Note, however, that although the portfolio valuation exception must be applied consistently, it may be appropriate for an entity to change its policy decision if its risk preferences change. Paragraph BC59 of ASU 2011-04 addresses this issue:

The Boards decided to require a reporting entity to provide evidence that it manages its net risk exposure consistently from period to period. The Boards decided this because a reporting entity that can provide evidence that it manages its financial instruments on the basis of its net risk exposure would do so consistently for a particular portfolio from period to period, and not on a net basis for that portfolio in some periods and on a gross basis in other periods. Some respondents found that requirement limiting because they noted that the composition of a portfolio changes continually as the reporting entity rebalances the portfolio and changes its risk exposure preferences over time. Although the reporting entity does not need to maintain a static portfolio, the Boards decided to clarify that the reporting entity must make an accounting policy decision to use the exception described in paragraphs BC56 and BC57. The Boards also decided that the accounting policy decision could be changed if the reporting entity's risk exposure preferences change. In that case, the reporting entity can decide not to use the exception but instead to measure the fair value of its financial instruments on an individual instrument basis. However, if the reporting entity continues to value a portfolio using the exception, it must do so consistently from period to period. [Emphasis added]

If an entity's risk exposure preferences change and the entity no longer applies the portfolio valuation exception as an accounting policy, the change does not represent a change in accounting principle under ASC 250; rather, it would generally reflect the application of U.S. GAAP to different facts and circumstances. Nevertheless, we believe that once the policy election is made, changes would be infrequent and would be necessitated by either significant changes in facts and circumstances or a conclusion that the conditions for applying the portfolio valuation exception are no longer met.
See Sections 10.2.8.2 and 10.2.8.3 for discussion of the nature of the risks that qualify for the portfolio valuation exception and the price within a bid-ask spread that is used to value a portfolio under this exception. See Example 10-16 for an illustration of the application of the portfolio valuation exception.

**Changing Lanes**

ASU 2018-09 amended ASC 820-10-35-18D to provide for a unit of valuation on the basis of a group that includes, in addition to financial assets and financial liabilities, nonfinancial items accounted for as derivatives in accordance with ASC 815, or combinations of these items. Before this amendment, this exception related to the unit of valuation was only allowed for groups of financial assets and financial liabilities with offsetting risk exposures. ASU 2018-09 only changed the nature of the items eligible for the portfolio valuation exception. All the other guidance related to this exception was unchanged.

### 10.2.8.1.1 Disclosure

ASC 820-10-50-2D requires entities that make an accounting policy decision to use the portfolio valuation exception in ASC 820-10-35-18D to disclose that fact. See further discussion in Sections 11.2.2.1 and 11.3.2.1. Section 11.2.3.5.5 discusses the allocation of portfolio-level adjustments to the individual items within a portfolio.

### 10.2.8.2 Exposure to Market Risks

**ASC 820-10**

**Exposure to Market Risks**

35-18I When using the exception in paragraph 820-10-35-18D to measure the fair value of a group of financial assets and financial liabilities managed on the basis of the reporting entity's net exposure to a particular market risk (or risks), the reporting entity shall apply the price within the bid-ask spread that is most representative of fair value in the circumstances to the reporting entity's net exposure to those market risks (see paragraphs 820-10-35-36C through 35-36D).

**Pending Content (Transition Guidance: ASC 105-10-65-5)**

35-18I When using the exception in paragraph 820-10-35-18D to measure the fair value of a group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items managed on the basis of the reporting entity's net exposure to a particular market risk (or risks), the reporting entity shall apply the price within the bid-ask spread that is most representative of fair value in the circumstances to the reporting entity's net exposure to those market risks (see paragraphs 820-10-35-36C through 35-36D).

35-18J When using the exception in paragraph 820-10-35-18D, a reporting entity shall ensure that the market risk (or risks) to which the reporting entity is exposed within that group of financial assets and financial liabilities is substantially the same. For example, a reporting entity would not combine the interest rate risk associated with a financial asset with the commodity price risk associated with a financial liability, because doing so would not mitigate the reporting entity's exposure to interest rate risk or commodity price risk. When using the exception in paragraph 820-10-35-18D, any basis risk resulting from the market risk parameters not being identical shall be taken into account in the fair value measurement of the financial assets and financial liabilities within the group.
The ASC master glossary defines “market risk” as comprising interest rate risk, currency risk, and other price risk. To apply the portfolio valuation exception in ASC 820-10-35-18D, an entity must ensure that the particular market risk of the eligible items for which the exception is being applied are substantially the same. In doing so, the entity must consider both the nature and duration of the relevant market risk. Thus, the portfolio valuation exception should only be applied to a portfolio that includes eligible assets and liabilities for which the type of market risk is the same and that share that market risk for a similar period. It would be inappropriate to establish a portfolio that contains assets and liabilities subject to different market risks (i.e., different types of market risks or different durations of the same type of market risk) because of the lack of risk exposure mitigation. However, as indicated in ASC 820-10-35-18K, an entity could potentially measure an exposure to a particular type of market risk on a partial-net, partial-gross basis so that duration risk is appropriately taken into account.

When the portfolio valuation exception is applied to a portfolio of eligible items with offsetting market risks, an entity applies the guidance in ASC 820-10-35-36C and 35-36D to determine the price within the bid-ask spread that is most representative of the fair value of the portfolio (i.e., the net price to sell or transfer the portfolio). See Section 10.4.4 for discussion of the use of mid-market pricing as a practical expedient. See also Section 10.4.3.3 for discussion of the use of blockage factors when the portfolio valuation exception is applied.
10.2.8.3 Exposure to the Credit Risk of a Particular Counterparty

ASC 820-10

Exposure to the Credit Risk of a Particular Counterparty

35-18L When using the exception in paragraph 820-10-35-18D to measure the fair value of a group of financial assets and financial liabilities entered into with a particular counterparty, the reporting entity shall include the effect of the reporting entity's net exposure to the credit risk of that counterparty or the counterparty's net exposure to the credit risk of the reporting entity in the fair value measurement when market participants would take into account any existing arrangements that mitigate credit risk exposure in the event of default (for example, a master netting agreement with the counterparty or an agreement that requires the exchange of collateral on the basis of each party's net exposure to the credit risk of the other party). The fair value measurement shall reflect market participants' expectations about the likelihood that such an arrangement would be legally enforceable in the event of default.

Pending Content (Transition Guidance: ASC 105-10-65-5)

35-18L When using the exception in paragraph 820-10-35-18D to measure the fair value of a group of financial assets, financial liabilities, items accounted for as derivatives in accordance with Topic 815, or combinations of these items entered into with a particular counterparty, the reporting entity shall include the effect of the reporting entity's net exposure to the credit risk of that counterparty or the counterparty's net exposure to the credit risk of the reporting entity in the fair value measurement when market participants would take into account any existing arrangements that mitigate credit risk exposure in the event of default (for example, a master netting agreement with the counterparty or an agreement that requires the exchange of collateral on the basis of each party's net exposure to the credit risk of the other party). The fair value measurement shall reflect market participants' expectations about the likelihood that such an arrangement would be legally enforceable in the event of default.

In addition to being applicable to offsetting positions in market risk, the portfolio valuation exception in ASC 820-10-35-18D can be used for a portfolio of eligible assets and liabilities entered into with a single counterparty so that this portfolio can be valued on the basis of the entity's net exposure to the counterparty's credit risk or the net exposure of the counterparty's credit risk to the entity provided that market participants would take into account existing arrangements between the parties that mitigate credit risk exposure (e.g., collateral posting or master netting arrangements). In this circumstance, the individual eligible assets and liabilities must be with the same counterparty but do not need to share the same exposures to market risk. Those assets and liabilities are first measured at fair value, with the exception of consideration of credit risk. The portfolio valuation exception is then applied to measure the net credit risk of the portfolio. The determination of the net credit risk valuation adjustment should take into account the relevant arrangements between the parties that result in a mitigation of credit risk. Such portfolio-level credit risk valuation adjustments must be allocated to the individual assets and liabilities within the portfolio (see Section 11.2.3.5.5 for more information about such allocations).
10.3 Valuation Techniques

10.3.1 General

ASC 820-10

Valuation Techniques

35-24 A reporting entity shall use valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

35-24A The objective of using a valuation technique is to estimate the price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions. Three widely used valuation approaches are the market approach, cost approach, and income approach. The main aspects of valuation techniques consistent with those approaches are summarized in paragraphs 820-10-55-3A through 55-3G. An entity shall use valuation techniques consistent with one or more of those approaches to measure fair value.

35-27 The Examples in Section 820-10-55 illustrate the judgments that might apply when a reporting entity measures assets and liabilities at fair value in different valuation situations.

Fair Value Hierarchy

35-38 The availability of relevant inputs and their relative subjectivity might affect the selection of appropriate valuation techniques (see paragraph 820-10-35-24). However, the fair value hierarchy prioritizes the inputs to valuation techniques, not the valuation techniques used to measure fair value. For example, a fair value measurement developed using a present value technique might be categorized within Level 2 or Level 3, depending on the inputs that are significant to the entire measurement and the level of the fair value hierarchy within which those inputs are categorized.

ASC 820-10 — Glossary

Cost Approach

A valuation approach that reflects the amount that would be required currently to replace the service capacity of an asset (often referred to as current replacement cost).

Income Approach

Valuation approaches that convert future amounts (for example, cash flows or income and expenses) to a single current (that is, discounted) amount. The fair value measurement is determined on the basis of the value indicated by current market expectations about those future amounts.

Market Approach

A valuation approach that uses prices and other relevant information generated by market transactions involving identical or comparable (that is, similar) assets, liabilities, or a group of assets and liabilities, such as a business.

An entity must use judgment, and will often need to engage valuation specialists, to determine the appropriate valuation technique(s) for measuring the fair value of an asset, liability, or equity instrument in accordance with ASC 820. This determination will often depend on the nature of the item being valued. As discussed in Section 10.3.2, an entity may determine that it is appropriate to use multiple valuation techniques to measure the fair value of an asset, liability, or equity instrument. Further, as discussed in ASC 820-10-35-38, an entity should consider the observability of the inputs into a specific valuation technique in determining which technique(s) to use.
ASC 820-10-55-3A through 55-3G below describe three widely used valuation techniques — the market approach, cost approach, and income approach.

**ASC 820-10**

*Market Approach*

**55-3A** The market approach uses prices and other relevant information generated by market transactions involving identical or comparable (that is, similar) assets, liabilities, or a group of assets and liabilities, such as a business.

**55-3B** For example, valuation techniques consistent with the market approach often use market multiples derived from a set of comparables. Multiples might be in ranges with a different multiple for each comparable. The selection of the appropriate multiple within the range requires judgment, considering qualitative and quantitative factors specific to the measurement.

**55-3C** Valuation techniques consistent with the market approach include matrix pricing. Matrix pricing is a mathematical technique used principally to value some types of financial instruments, such as debt securities, without relying exclusively on quoted prices for the specific securities, but rather relying on the securities' relationship to other benchmark quoted securities.

*Cost Approach*

**55-3D** The cost approach reflects the amount that would be required currently to replace the service capacity of an asset (often referred to as current replacement cost).

**55-3E** From the perspective of a market participant seller, the price that would be received for the asset is based on the cost to a market participant buyer to acquire or construct a substitute asset of comparable utility, adjusted for obsolescence. That is because a market participant buyer would not pay more for an asset than the amount for which it could replace the service capacity of that asset. Obsolescence encompasses physical deterioration, functional (technological) obsolescence, and economic (external) obsolescence and is broader than depreciation for financial reporting purposes (an allocation of historical cost) or tax purposes (using specified service lives). In many cases, the current replacement cost method is used to measure the fair value of tangible assets that are used in combination with other assets or with other assets and liabilities.

*Income Approach*

**55-3F** The income approach converts future amounts (for example, cash flows or income and expenses) to a single current (that is, discounted) amount. When the income approach is used, the fair value measurement reflects current market expectations about those future amounts.

**55-3G** Those valuation techniques include, for example, the following:

- Present value techniques
- Option-pricing models, such as the Black-Scholes-Merton formula or a binomial model (that is, a lattice model), that incorporate present value techniques and reflect both the time value and the intrinsic value of an option
- The multiperiod excess earnings method, which is used to measure the fair value of some intangible assets.
10.3.1.1 **Present Value Techniques**

**ASC 820-10**

Present Value Techniques

**55-4** Paragraphs 820-10-55-5 through 55-20 describe the use of present value techniques to measure fair value. Those paragraphs focus on a discount rate adjustment technique and an expected cash flow (expected present value) technique. Those paragraphs neither prescribe the use of a single specific present value technique nor limit the use of present value techniques to measure fair value to the techniques discussed. The present value technique used to measure fair value will depend on facts and circumstances specific to the asset or liability being measured (for example, whether prices for comparable assets or liabilities can be observed in the market) and the availability of sufficient data.

The Components of a Present Value Measurement

**55-5** Present value (that is, an application of the income approach) is a tool used to link future amounts (for example, cash flows or values) to a present amount using a discount rate. A fair value measurement of an asset or a liability using a present value technique captures all of the following elements from the perspective of market participants at the measurement date:

a. An estimate of future cash flows for the asset or liability being measured.

b. Expectations about possible variations in the amount and timing of the cash flows representing the uncertainty inherent in the cash flows.

c. The time value of money, represented by the rate on risk-free monetary assets that have maturity dates or durations that coincide with the period covered by the cash flows and pose neither uncertainty in timing nor risk of default to the holder (that is, a risk-free interest rate). For present value computations denominated in nominal U.S. dollars, the yield curve for U.S. Treasury securities determines the appropriate risk-free interest rate.

d. The price for bearing the uncertainty inherent in the cash flows (that is, a risk premium).

e. Other factors that market participants would take into account in the circumstances.

f. For a liability, the nonperformance risk relating to that liability, including the reporting entity's (that is, the obligor's) own credit risk.

General Principles

**55-6** Present value techniques differ in how they capture the elements in the preceding paragraph. However, all of the following general principles govern the application of any present value technique used to measure fair value:

a. Cash flows and discount rates should reflect assumptions that market participants would use when pricing the asset or liability.

b. Cash flows and discount rates should take into account only the factors attributable to the asset or liability being measured.

c. To avoid double counting or omitting the effects of risk factors, discount rates should reflect assumptions that are consistent with those inherent in the cash flows. For example, a discount rate that reflects the uncertainty in expectations about future defaults is appropriate if using contractual cash flows of a loan (that is, a discount rate adjustment technique). That same rate should not be used if using expected (that is, probability-weighted) cash flows (that is, an expected present value technique) because the expected cash flows already reflect assumptions about the uncertainty in future defaults; instead, a discount rate that is commensurate with the risk inherent in the expected cash flows should be used.
d. Assumptions about cash flows and discount rates should be internally consistent. For example, nominal cash flows, which include the effect of inflation, should be discounted at a rate that includes the effect of inflation. The nominal risk-free interest rate includes the effect of inflation. Real cash flows, which exclude the effect of inflation, should be discounted at a rate that excludes the effect of inflation. Similarly, after-tax cash flows should be discounted using an after-tax discount rate. Pretax cash flows should be discounted at a rate consistent with those cash flows.

e. Discount rates should be consistent with the underlying economic factors of the currency in which the cash flows are denominated.

Risk and Uncertainty

55-7 A fair value measurement using present value techniques is made under conditions of uncertainty because the cash flows used are estimates rather than known amounts. In many cases, both the amount and timing of the cash flows are uncertain. Even contractually fixed amounts, such as the payments on a loan, are uncertain if there is risk of default.

55-8 Market participants generally seek compensation (that is, a risk premium) for bearing the uncertainty inherent in the cash flows of an asset or a liability. A fair value measurement should include a risk premium reflecting the amount that market participants would demand as compensation for the uncertainty inherent in the cash flows. Otherwise, the measurement would not faithfully represent fair value. In some cases, determining the appropriate risk premium might be difficult. However, the degree of difficulty alone is not a sufficient reason to exclude a risk premium.

55-9 Present value techniques differ in how they adjust for risk and in the type of cash flows they use. For example:

a. The discount rate adjustment technique (see paragraphs 820-10-55-10 through 55-12) uses a risk-adjusted discount rate and contractual, promised, or most likely cash flows.

b. Method 1 of the expected present value technique (see paragraph 820-10-55-15) uses risk-adjusted expected cash flows and a risk-free rate.

c. Method 2 of the expected present value technique (see paragraph 820-10-55-16) uses expected cash flows that are not risk adjusted and a discount rate adjusted to include the risk premium that market participants require. That rate is different from the rate used in the discount rate adjustment technique.

Discount Rate Adjustment Technique

55-10 The discount rate adjustment technique uses a single set of cash flows from the range of possible estimated amounts, whether contractual or promised (as is the case for a bond) or most likely cash flows. In all cases, those cash flows are conditional upon the occurrence of specified events (for example, contractual or promised cash flows for a bond are conditional on the event of no default by the debtor). The discount rate used in the discount rate adjustment technique is derived from observed rates of return for comparable assets or liabilities that are traded in the market. Accordingly, the contractual, promised, or most likely cash flows are discounted at an observed or estimated market rate for such conditional cash flows (that is, a market rate of return).

55-11 The discount rate adjustment technique requires an analysis of market data for comparable assets or liabilities. Comparability is established by considering the nature of the cash flows (for example, whether the cash flows are contractual or noncontractual and are likely to respond similarly to changes in economic conditions), as well as other factors (for example, credit standing, collateral, duration, restrictive covenants, and liquidity). Alternatively, if a single comparable asset or liability does not fairly reflect the risk inherent in the cash flows of the asset or liability being measured, it may be possible to derive a discount rate using data for several comparable assets or liabilities in conjunction with the risk-free yield curve (that is, using a build-up methodology). Paragraph 820-10-55-33 illustrates the build-up methodology.
When the discount rate adjustment technique is applied to fixed receipts or payments, the adjustment for risk inherent in the cash flows of the asset or liability being measured is included in the discount rate. In some applications of the discount rate adjustment technique to cash flows that are not fixed receipts or payments, an adjustment to the cash flows may be necessary to achieve comparability with the observed asset or liability from which the discount rate is derived.

**Expected Present Value Technique**

The expected present value technique uses as a starting point a set of cash flows that represents the probability-weighted average of all possible future cash flows (that is, the expected cash flows). The resulting estimate is identical to expected value, which, in statistical terms, is the weighted average of a discrete random variable's possible values with the respective probabilities as the weights. Because all possible cash flows are probability-weighted, the resulting expected cash flow is not conditional upon the occurrence of any specified event (unlike the cash flows used in the discount rate adjustment technique).

In making an investment decision, risk-averse market participants would take into account the risk that the actual cash flows may differ from the expected cash flows. Portfolio theory distinguishes between two types of risk:

a. Unsystematic (diversifiable) risk
b. Systematic (nondiversifiable) risk.

Method 1 of the expected present value technique adjusts the expected cash flows of an asset for systematic (that is, market) risk by subtracting a cash risk premium (that is, risk-adjusted expected cash flows). Those risk-adjusted expected cash flows represent a certainty equivalent cash flow, which is discounted at a risk-free interest rate. A certainty equivalent cash flow refers to an expected cash flow (as defined), adjusted for risk so that a market participant is indifferent to trading a certain cash flow for an expected cash flow. For example, if a market participant was willing to trade an expected cash flow of $1,200 for a certain cash flow of $1,000, the $1,000 is the certainty equivalent of the $1,200 (that is, the $200 would represent the cash risk premium). In that case, the market participant would be indifferent as to the asset held.

In contrast, Method 2 of the expected present value technique adjusts for systematic (that is, market) risk by applying a risk premium to the risk-free interest rate. Accordingly, the expected cash flows are discounted at a rate that corresponds to an expected rate associated with probability-weighted cash flows (that is, an expected rate of return). Models used for pricing risky assets, such as the capital asset pricing model, can be used to estimate the expected rate of return. Because the discount rate used in the discount rate adjustment technique is a rate of return relating to conditional cash flows, it is likely to be higher than the discount rate used in Method 2 of the expected present value technique, which is an expected rate of return relating to expected or probability-weighted cash flows.

To illustrate Methods 1 and 2, assume that an asset has expected cash flows of $780 in 1 year determined on the basis of the possible cash flows and probabilities shown below. The applicable risk-free interest rate for cash flows with a 1-year horizon is 5 percent, and the systematic risk premium for an asset with the same risk profile is 3 percent.

<table>
<thead>
<tr>
<th>Possible Cash Flows</th>
<th>Probability</th>
<th>Probability-Weighted Cash Flows</th>
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<tbody>
<tr>
<td>$ 500</td>
<td>15%</td>
<td>$ 75</td>
</tr>
<tr>
<td>$ 800</td>
<td>60%</td>
<td>$ 480</td>
</tr>
<tr>
<td>$ 900</td>
<td>25%</td>
<td>$ 225</td>
</tr>
<tr>
<td>Expected cash flows</td>
<td></td>
<td>$ 780</td>
</tr>
</tbody>
</table>
55-18 In this simple illustration, the expected cash flows ($780) represent the probability-weighted average of the 3 possible outcomes. In more realistic situations, there could be many possible outcomes. However, to apply the expected present value technique, it is not always necessary to take into account distributions of all possible cash flows using complex models and techniques. Rather, it might be possible to develop a limited number of discrete scenarios and probabilities that capture the array of possible cash flows. For example, a reporting entity might use realized cash flows for some relevant past period, adjusted for changes in circumstances occurring subsequently (for example, changes in external factors, including economic or market conditions, industry trends, and competition as well as changes in internal factors affecting the reporting entity more specifically), taking into account the assumptions of market participants.

55-19 In theory, the present value (that is, the fair value) of the asset's cash flows is the same whether determined using Method 1 or Method 2, as follows:

a. Using Method 1, the expected cash flows are adjusted for systematic (that is, market) risk. In the absence of market data directly indicating the amount of the risk adjustment, such adjustment could be derived from an asset pricing model using the concept of certainty equivalents. For example, the risk adjustment (that is, the cash risk premium of $22) could be determined using the systematic risk premium of 3 percent ($780 – [$780 × (1.05/1.08)]), which results in risk-adjusted expected cash flows of $758 ($780 – $22). The $758 is the certainty equivalent of $780 and is discounted at the risk-free interest rate (5 percent). The present value (that is, the fair value) of the asset is $722 ($758/1.05).

b. Using Method 2, the expected cash flows are not adjusted for systematic (that is, market) risk. Rather, the adjustment for that risk is included in the discount rate. Thus, the expected cash flows are discounted at an expected rate of return of 8 percent (that is, the 5 percent risk-free interest rate plus the 3 percent systematic risk premium). The present value (that is, the fair value) of the asset is $722 ($780/1.08).

55-20 When using an expected present value technique to measure fair value, either Method 1 or Method 2 could be used. The selection of Method 1 or Method 2 will depend on facts and circumstances specific to the asset or liability being measured, the extent to which sufficient data are available, and the judgments applied.

Example 2: Discount Rate Adjustment Technique — The Build-Up Methodology

55-33 To illustrate a build-up methodology (as discussed in paragraph 820-10-55-11), assume that Asset A is a contractual right to receive $800 in 1 year (that is, there is no timing uncertainty). There is an established market for comparable assets, and information about those assets, including price information, is available. Of those comparable assets:

a. Asset B is a contractual right to receive $1,200 in 1 year and has a market price of $1,083. Thus, the implied annual rate of return (that is, a 1-year market rate of return) is 10.8 percent ([($1,200/$1,083) – 1].

b. Asset C is a contractual right to receive $700 in 2 years and has a market price of $566. Thus, the implied annual rate of return (that is, a 2-year market rate of return) is 11.2 percent ([($700/$566)^0.5 – 1].

c. All three assets are comparable with respect to risk (that is, dispersion of possible payoffs and credit).

55-34 On the basis of the timing of the contractual payments to be received for Asset A relative to the timing for Asset B and Asset C (that is, one year for Asset B versus two years for Asset C), Asset B is deemed more comparable to Asset A. Using the contractual payment to be received for Asset A ($800) and the 1-year market rate derived from Asset B (10.8 percent), the fair value of Asset A is $722 ($800/1.108). Alternatively, in the absence of available market information for Asset B, the one-year market rate could be derived from Asset C using the build-up methodology. In that case, the 2-year market rate indicated by Asset C (11.2 percent) would be adjusted to a 1-year market rate using the term structure of the risk-free yield curve. Additional information and analysis might be required to determine whether the risk premiums for one-year and two-year assets are the same. If it is determined that the risk premiums for one-year and two-year assets are not the same, the two-year market rate of return would be further adjusted for that effect.
ASC 820-10-55-4 through 55-20 contain guidance on the application of present value techniques (i.e., an income approach). An entity should consider such guidance, which is derived from FASB Concepts Statement 7, when measuring the fair value of an asset, liability, or equity instrument on the basis of future cash flows. In addition, ASC 820-10-55-33 and 55-34 contain an example illustrating the application of a discount-rate adjustment technique. See also the examples in Section 10.2.7.5 and Section 10.6.4. For discussion of the valuation technique applied to determine the fair value of a customer-relationship intangible asset, see Section 10.10.4.

### 10.3.2 Using a Single Technique or Multiple Techniques

<table>
<thead>
<tr>
<th>ASC 820-10</th>
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<tbody>
<tr>
<td><strong>Valuation Techniques</strong></td>
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<tr>
<td>35-24B</td>
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In some cases, it is appropriate to use more than one valuation technique to determine the fair value of an asset, liability, or instrument classified in stockholders' equity. An entity that employs multiple valuation techniques should consider both supporting and contradictory evidence in determining the relevancy of the results of the individual techniques. An entity must use judgment to determine the “weighting” to give to each valuation technique used. When evaluating the reasonableness of the range of values arrived at by using multiple techniques, an entity should consider a value to be more reasonable if it is produced by a technique that maximizes the use of observable inputs and minimizes the use of unobservable inputs. For each measurement calculated, the entity must consider the fair value hierarchy and choose the most reliable input available. When two or more sources for the same input are in the same level of the fair value hierarchy, the entity chooses the source that reflects the least amount of subjectivity and that provides the most reliable information for the given input.

The FASB did not intend for Statement 157 to require the use of multiple valuation techniques; rather, the Board wanted to suggest that in certain situations, it may be necessary to use multiple techniques to determine fair value, as discussed in paragraphs C54 through C56 of Statement 157:

The Board affirmed that its intent was not to require the use of multiple valuation techniques. To convey its intent more clearly, the Board clarified that, consistent with existing valuation practice, valuation techniques that are appropriate in the circumstances and for which sufficient data are available should be used to measure fair value. This Statement does not specify the valuation technique that should be used in any particular circumstances. Determining the appropriateness of valuation techniques in the circumstances requires judgment.

The Exposure Draft referred to the cost and effort involved in obtaining the information used in a particular valuation technique as a basis for determining whether to use that valuation technique. Some respondents pointed out that the most appropriate valuation technique also might be the most costly valuation technique and that cost and effort should not be a basis for determining whether to use that valuation technique. Moreover, a cost-and-effort criterion likely would not be consistently applied. The Board agreed and removed that cost-and-effort criterion from this Statement.

The Board expects that in some cases, a single valuation technique will be used. In other cases, multiple valuation techniques will be used, and the results of those techniques evaluated and weighted, as appropriate, in determining fair value. The Board acknowledged that valuation techniques will differ, depending on the asset or liability and the availability of data. However, in all cases, the objective is to use the valuation technique (or combination of valuation techniques) that is appropriate in the circumstances and for which there are sufficient data.
Example 10-13 illustrates factors to consider in the determination of whether multiple valuation techniques should be used to measure fair value.

**Example 10-13**

**Use of Multiple Valuation Techniques**

Entity L, a private equity firm, is required to account for its investments at fair value on a recurring basis in accordance with ASC 946. Entity L holds a number of investments, two of which are in the common stock of:

- Company A, a clothing retailer that operates in a niche market of the baby clothing industry. Quoted prices are not available for A's stock, and most of A's competitors are either privately held or subsidiaries of larger publicly traded clothing retailers. Company A is similar to two other organizations whose shares are thinly traded in an observable market.

- Company B, a retailer that operates in the competitive consumer electronics industry. Although quoted prices are not available for B's stock, B is considered comparable to many companies whose shares are actively traded.

Entities commonly use the market approach and income approach to value equity investments that are not publicly traded. Under the market approach, entities use prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities, including a business (e.g., market-multiple approach). Under the income approach, entities use valuation techniques to convert future amounts to a single present amount (e.g., discounted cash flows model). Generally, the cost approach is not relevant to the valuation of equity investments.

Entity L should evaluate each investment individually to determine the appropriate valuation technique(s) used to measure fair value. Whether L should use both a market approach and an income approach to calculate the fair value of each investment (as opposed to using only a single valuation technique) depends on the facts and circumstances and could change over time.

Some factors that L should consider in evaluating the appropriateness of valuation techniques, including whether a single technique or multiple techniques should be employed, include the following:

- **Relevance and applicability of the technique** — Since the cost approach is not relevant to the valuation of equity investments, only valuation techniques that reflect market and income approaches should be considered. The appropriateness of each specific valuation technique will depend on the facts and circumstances. While L would assess the appropriateness of each valuation technique individually, it would also compare the techniques to each other.

- **Availability and reliability of data** — If L, for example, does not have sufficient reliable data to support an income approach but does have sufficient reliable data to support a market approach, a single approach (market approach) might be appropriate.

- **Comparative level of the alternative approaches in the fair value hierarchy** — L should determine the level in the ASC 820 fair value hierarchy in which (1) each input to each technique would be classified and (2) each measurement would fall in its entirety. For example, L may conclude that a single approach (market approach) is appropriate if it uses (1) a market approach based entirely on market-observable inputs, which places the fair value measurement in Level 2 in its entirety, and (2) the income approach, which in this example includes an unobservable input that is significant to the entire measurement and causes the measurement to be categorized in Level 3 of the fair value hierarchy. On the other hand, if both measurements are Level 3, L may conclude, after considering other factors, that it could use both approaches. However, to support the unobservable inputs used, it would still evaluate the availability and reliability of data. Even when all inputs are unobservable, L would choose the most reliable data available and the measurement technique or techniques that use the most reliable data available after it considers all inputs significant to the measurement.

As discussed above, when evaluating the reasonableness of the range of values arrived at by using multiple techniques, L should consider a value to be more reasonable if it is produced by a technique that maximizes the use of observable inputs and minimizes the use of unobservable inputs.
Example 10-13 (continued)

- **Significant decline in volume and level of market activity** — If, on the basis of ASC 820-10-35-54C, L concludes that there has been a significant decline in volume and level of market activity relative to normal market activity for the investment being measured, it might be appropriate for L to change its valuation technique (e.g., shift from a market approach to an income approach) or use multiple valuation techniques (e.g., use both an income approach and a market approach) in determining fair value. However, regardless of the technique(s) used, the resulting fair value measurement must reflect market-participant assumptions under current market conditions.

- **Views of market participants on the relevance of valuation techniques** — Market transactions involving the specific investment or similar investments may highlight the use of a single technique or multiple techniques by market participants. Entity L may observe approaches used by market participants to help them determine a bid price for similar investments (i.e., through discussions with other private equity firms or valuation specialists) and to gain an understanding of techniques that are used by market participants in determining the fair value at which they will transact.

Entity L should consider the above factors in identifying an appropriate approach for measuring the fair value of its investment in A. For example, assume that when using a market approach, L estimates that market participants would incorporate significant entity-specific adjustments into the valuation of A’s stock (e.g., risk adjustments for illiquidity/uncertainty of A’s stock relative to that of comparable companies as well as other adjustments to reflect business model differences between A and comparable companies). These adjustments are calculated on the basis of L’s assumptions, rendering the fair value measurement Level 3. Similarly, assume that in using an income approach based on discounted cash flows to measure fair value, L must make significant entity-specific assumptions in forecasting A’s future cash flows. In such a case, the fair value measurement under the income approach is also Level 3.

In addition, because (1) the cost approach would not be relevant and (2) the market and income approaches are common valuation techniques used by prospective buyers to help them bid on acquisitions, L would generally conclude that both valuation techniques are appropriate in this circumstance. Further, it should use both approaches in estimating fair value (even if one approach is only used to corroborate the results of the other) provided that relevant and reliable inputs are available and there are no other factors that would cause L to conclude that one of the approaches is superior.

Likewise, in determining an appropriate approach for measuring the fair value of its investment in B, L should consider the above factors. For example, assume that when using a market approach, L estimates that market participants would not incorporate significant adjustments into the valuation of B’s stock, resulting in a Level 2 measurement (e.g., because of the large number of similar companies and high trading volume of the comparable companies’ stock). Similarly, assume that when measuring fair value by using an income approach based on discounted cash flows, L must use significant entity-specific assumptions in forecasting B’s future cash flows. These assumptions would result in a Level 3 fair value measurement under the income approach.

As a result, L may conclude that using a single valuation technique (e.g., market approach) may be appropriate in this circumstance because it results in a more reliable fair value measurement (Level 2 vs. Level 3). (Note that in practice it may not be common that an entity is not required to incorporate significant adjustments into a market approach to value an equity investment; this example is intended to illustrate the concept of maximizing the use of relevant observable inputs in a fair value measurement.)

Entity L should also consider using a valuation specialist, when appropriate, and should document its conclusions and considerations related to the application of valuation techniques (as part of its internal control policies and procedures).
Cases A and B of Example 3 in ASC 820 also illustrate the use of multiple valuation techniques.

**ASC 820-10**

**Case A: Machine Held and Used**

55-36 A reporting entity acquires a machine in a business combination. The machine will be held and used in its operations. The machine was originally purchased by the acquired entity from an outside vendor and, before the business combination, was customized by the acquired entity for use in its operations. However, the customization of the machine was not extensive. The acquiring entity determines that the asset would provide maximum value to market participants through its use in combination with other assets or with other assets and liabilities (as installed or otherwise configured for use). There is no evidence to suggest that the current use of the machine is not its highest and best use. Therefore, the highest and best use of the machine is its current use in combination with other assets or with other assets and liabilities.

55-37 The reporting entity determines that sufficient data are available to apply the cost approach and, because the customization of the machine was not extensive, the market approach. The income approach is not used because the machine does not have a separately identifiable income stream from which to develop reliable estimates of future cash flows. Furthermore, information about short-term and intermediate-term lease rates for similar used machinery that otherwise could be used to project an income stream (that is, lease payments over remaining service lives) is not available. The market and cost approaches are applied as follows:

- a. The market approach is applied using quoted prices for similar machines adjusted for differences between the machine (as customized) and the similar machines. The measurement reflects the price that would be received for the machine in its current condition (used) and location (installed and configured for use). The fair value indicated by that approach ranges from $40,000 to $48,000.
- b. The cost approach is applied by estimating the amount that would be required currently to construct a substitute (customized) machine of comparable utility. The estimate takes into account the condition of the machine and the environment in which it operates, including physical wear and tear (that is, physical deterioration), improvements in technology (that is, functional obsolescence), conditions external to the condition of the machine such as a decline in the market demand for similar machines (that is, economic obsolescence), and installation costs. The fair value indicated by that approach ranges from $40,000 to $52,000.

55-38 The reporting entity determines that the higher end of the range indicated by the market approach is most representative of fair value and, therefore, ascribes more weight to the results of the market approach. That determination is made on the basis of the relative subjectivity of the inputs, taking into account the degree of comparability between the machine and the similar machines. In particular:

- a. The inputs used in the market approach (quoted prices for similar machines) require fewer and less subjective adjustments than the inputs used in the cost approach.
- b. The range indicated by the market approach overlaps with, but is narrower than, the range indicated by the cost approach.
- c. There are no known unexplained differences (between the machine and the similar machines) within that range.

Accordingly, the reporting entity determines that the fair value of the machine is $48,000.

55-38A If customization of the machine was extensive or if there were not sufficient data available to apply the market approach (for example, because market data reflect transactions for machines used on a standalone basis, such as, a scrap value for specialized assets, rather than machines used in combination with other assets or with other assets and liabilities), the reporting entity would apply the cost approach. When an asset is used in combination with other assets or with other assets and liabilities, the cost approach assumes the sale of the machine to a market participant buyer with the complementary assets and the associated liabilities. The price received for the sale of the machine (that is, an exit price) would not be more than either of the following:

- a. The cost that a market participant buyer would incur to acquire or construct a substitute machine of comparable utility
- b. The economic benefit that a market participant buyer would derive from the use of the machine.
Case B: Software Asset

55-39 A reporting entity acquires a group of assets. The asset group includes an income-producing software asset internally developed for licensing to customers and its complementary assets (including a related database with which the software asset is used) and the associated liabilities. To allocate the cost of the group to the individual assets acquired, the reporting entity measures the fair value of the software asset. The reporting entity determines that the software asset would provide maximum value to market participants through its use in combination with other assets or with other assets and liabilities (that is, its complementary assets and the associated liabilities). There is no evidence to suggest that the current use of the software asset is not its highest and best use. Therefore, the highest and best use of the software asset is its current use. (In this case, the licensing of the software asset, in and of itself, does not indicate that the fair value of the asset would be maximized through its use by market participants on a standalone basis.)

55-40 The reporting entity determines that, in addition to the income approach, sufficient data might be available to apply the cost approach but not the market approach. Information about market transactions for comparable software assets is not available. The income and cost approaches are applied as follows:

a. The income approach is applied using a present value technique. The cash flows used in that technique reflect the income stream expected to result from the software asset (license fees from customers) over its economic life. The fair value indicated by that approach is $15 million.

b. The cost approach is applied by estimating the amount that currently would be required to construct a substitute software asset of comparable utility (that is, taking into account functional and economic obsolescence). The fair value indicated by that approach is $10 million.

55-41 Through its application of the cost approach, the reporting entity determines that market participants would not be able to construct a substitute software asset of comparable utility. Some characteristics of the software asset are unique, having been developed using proprietary information, and cannot be readily replicated. The reporting entity determines that the fair value of the software asset is $15 million, as indicated by the income approach.

10.3.3 Model Calibration

Valuation Techniques

35-24C If the transaction price is fair value at initial recognition and a valuation technique that uses unobservable inputs will be used to measure fair value in subsequent periods, the valuation technique shall be calibrated so that at initial recognition the result of the valuation technique equals the transaction price. Calibration ensures that the valuation technique reflects current market conditions, and it helps a reporting entity to determine whether an adjustment to the valuation technique is necessary (for example, there might be a characteristic of the asset or liability that is not captured by the valuation technique). After initial recognition, when measuring fair value using a valuation technique or techniques that use unobservable inputs, a reporting entity shall ensure that those valuation techniques reflect observable market data (for example, the price for a similar asset or liability) at the measurement date.
Section 9.3 discusses the requirement in ASC 820-10-35-24C to calibrate a valuation technique to the transaction price. While that discussion focuses primarily on calibration of a valuation technique to the initial amount recognized for an asset or liability that is subsequently measured at fair value, entities should also calibrate valuation techniques to other relevant transactions, such as:

- Observable market transactions (e.g., calibration of a valuation technique used to measure the fair value of mortgage servicing rights to observed market transactions involving the sale of mortgage servicing rights).
- An entity’s own sale transactions (e.g., calibration of a valuation technique used to measure fair value of private equity investments to amounts received upon disposition of such investments).

See Section 10.7 for discussion of how an entity considers whether observable transactions represent orderly transactions between market participants. See Section 10.8.2 for discussion of an entity’s use of quotes from brokers or pricing services to calibrate its valuation techniques.

### 10.3.4 Changes in Valuation Techniques

<table>
<thead>
<tr>
<th>ASC 820-10</th>
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<tbody>
<tr>
<td>Valuation Techniques</td>
</tr>
<tr>
<td>35-25 Valuation techniques used to measure fair value shall be applied consistently. However, a change in a valuation technique or its application (for example, a change in its weighting when multiple valuation techniques are used or a change in an adjustment applied to a valuation technique) is appropriate if the change results in a measurement that is equally or more representative of fair value in the circumstances. That might be the case if, for example, any of the following events take place:</td>
</tr>
<tr>
<td>a. New markets develop.</td>
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<tr>
<td>b. New information becomes available.</td>
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<tr>
<td>c. Information previously used is no longer available.</td>
</tr>
<tr>
<td>d. Valuation techniques improve.</td>
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<tr>
<td>e. Market conditions change.</td>
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<tr>
<td>35-26 Revisions resulting from a change in the valuation technique or its application shall be accounted for as a change in accounting estimate. (See paragraph 250-10-45-17. However, paragraph 250-10-50-5 explains that the disclosures in Topic 250 for a change in accounting estimate are not required for revisions resulting from a change in a valuation technique or its application.)</td>
</tr>
</tbody>
</table>

ASC 820 does not preclude an entity from changing its valuation technique or the application thereof. However, before making such a change, the entity must determine that doing so would yield a measurement that is equally or more representative of fair value. ASC 820-10-35-25 gives examples of circumstances in which an entity may need to change its valuation technique or how it applies such a technique.

A change in valuation technique from one in which a quoted price is used would generally not be appropriate when there is a quote from an active market for an identical asset. As discussed in ASC 820-10-35-41, if a quoted price in an active market exists, it “shall be used without adjustment to measure fair value whenever available,” with limited exceptions. Decreased volumes in a market are not necessarily indicative of an inactive market (see Section 10.6.2.1 for more information).
Depending on the circumstances, a change from a valuation technique in which a quoted price (or a direct adjustment to a quoted price) is used to a different valuation technique (e.g., a discounted cash flow technique) may be appropriate in the following cases:

- When a quoted price is no longer available.
- When a quoted price is available but the market is not active (see ASC 820-10-35-48(b)).

ASC 820-10-35-54C states that entities must “evaluate the significance and relevance” of the following factors to determine whether the volume or level of activity for an asset or liability has significantly decreased:

a. There are few recent transactions.

b. Price quotations are not developed using current information.

c. Price quotations vary substantially either over time or among market makers (for example, some brokered markets).

d. Indices that previously were highly correlated with the fair values of the asset or liability are demonstrably uncorrelated with recent indications of fair value for that asset or liability.

e. There is a significant increase in implied liquidity risk premiums, yields, or performance indicators . . . for observed transactions or quoted prices when compared with the reporting entity's estimate of expected cash flows, taking into account all available market data about credit and other nonperformance risk for the asset or liability.

f. There is a wide bid-ask spread or significant increase in the bid-ask spread.

g. There is a significant decline in the activity of, or there is an absence of, a market for new issues . . . for the asset or liability or similar assets or liabilities [or own equity instruments].

h. Little information is publicly available (for example, for transactions that take place in a principal-to-principal market).

Note, however, that an entity must consider prices from relevant observable transactions in determining fair value even if the market is not active. See Chapter 7 and Section 10.6.3 for more information.

- The entity is not able to access the price in the market in which it is quoted (see ASC 820-10-35-6B and ASC 820-10-35-41B(b)).

- The price is not based on relevant observable market data and does not reflect assumptions that market participants would make in pricing the asset as of the measurement date. (As discussed in Section 10.8, an entity cannot necessarily assume that a price provided by an external source is representative of fair value as of the measurement date.)

When there is no quoted price in an active market, it is sometimes appropriate for an entity to use multiple valuation techniques to measure fair value (as discussed in ASC 820-10-35-24B). Like other changes in valuation technique, a change in the application of multiple valuation techniques (such as a change in how they are weighted) is permitted if it results in a measurement that is equally or more representative of fair value in the circumstances. For instance, if the entity employs both a market approach (e.g., market multiples for comparable assets) and an income approach (e.g., a discounted cash flow model) in determining fair value, the method of weighting the two approaches should be consistent over time unless the conditions for a change in valuation technique are met. Furthermore, an entity would consider the reasonableness of the range of fair value measurements resulting from the approaches. ASC 820-10-35-54F states that “[t]he objective is to determine the point within the range that is most representative of fair value under current market conditions. A wide range of fair value measurements may be an indication that further analysis is needed.”

ASC 820 also requires disclosure of the valuation techniques and inputs used to measure fair value as well as a discussion of changes in valuation techniques (including the justification for making them) during interim and annual periods (see ASC 820-10-50-2(bbb)). See Chapter 11 for more information.
10.4 Inputs to Valuation Techniques

10.4.1 General

ASC 820-10

General Principles

35-36 Valuation techniques used to measure fair value shall maximize the use of relevant observable inputs and minimize the use of unobservable inputs.

35-36A Examples of markets in which inputs might be observable for some assets and liabilities (for example, financial instruments) include exchange markets, dealer markets, brokered markets, and principal-to-principal markets.

35-36B A reporting entity shall select inputs that are consistent with the characteristics of the asset or liability that market participants would take into account in a transaction for the asset or liability (see paragraphs 820-10-35-2B through 35-2C). In some cases, those characteristics result in the application of an adjustment, such as a premium or discount (for example, a control premium or noncontrolling interest discount). However, a fair value measurement shall not incorporate a premium or discount that is inconsistent with the unit of account in the Topic that requires or permits the fair value measurement. Premiums or discounts that reflect size as a characteristic of the reporting entity's holding (specifically, a blockage factor that adjusts the quoted price of an asset or a liability because the market's normal daily trading volume is not sufficient to absorb the quantity held by the entity, as described in paragraph 820-10-35-44) rather than as a characteristic of the asset or liability (for example, a control premium when measuring the fair value of a controlling interest) are not permitted in a fair value measurement. In all cases, if there is a quoted price in an active market (that is, a Level 1 input) for an asset or a liability, a reporting entity shall use that quoted price without adjustment when measuring fair value, except as specified in paragraph 820-10-35-41C.

Under ASC 820, a fair value measurement should maximize the use of observable inputs and minimize the use of unobservable inputs. Furthermore, the inputs used in a valuation technique must be selected on the basis of the inputs that market participants in the principal (or most advantageous) market would select after considering the characteristics of the asset, liability, or equity-classified instrument that is being measured at fair value.

If an entity is using a valuation technique to determine fair value and has information indicating that market participants would use different inputs or assumptions, the entity cannot choose to rely on its own information in determining what inputs or assumptions to use, because a fair value measurement is market-based rather than entity-specific. These concepts are addressed in the definition of fair value as well as in a number of paragraphs in ASC 820 (e.g., ASC 820-10-05-1C, ASC 820-10-35-53, ASC 820-10-35-54A, and ASC 820-10-35-54E). For more information, see Section 8.4.2.2.

See Chapter 6 for further discussion of the principal or most advantageous market. See Chapter 7 for more information about market-participant assumptions.

10.4.2 Risk Adjustments When Significant Unobservable Inputs Are Used in Valuation Techniques

In accordance with the prioritization of inputs required by the fair value hierarchy, an entity's valuation technique should incorporate relevant observable inputs (i.e., Level 1 and 2 inputs) whenever they are available; however, if relevant observable inputs are not available, the entity uses unobservable inputs (i.e., Level 3 inputs). ASC 820-10-35-53 indicates that unobservable inputs must “reflect the assumptions that market participants would use when pricing” an asset, liability, or instrument classified in an entity's stockholders' equity. When using unobservable inputs, entities should consider whether risk
adjustments are necessary on the basis of whether market participants would require such adjustments. ASC 820-10-35-54 states:

Assumptions about risk include the risk inherent in a particular valuation technique used to measure fair value (such as a pricing model) and the risk inherent in the inputs to the valuation technique. A measurement that does not include an adjustment for risk would not represent a fair value measurement if market participants would include one when pricing the asset or liability. For example, it might be necessary to include a risk adjustment when there is significant measurement uncertainty (for example, when there has been a significant decrease in the volume or level of activity when compared with normal market activity for the asset or liability, or similar assets or liabilities, and the reporting entity has determined that the transaction price or quoted price does not represent fair value, as described in paragraphs 820-10-35-54C through 35-54J).

Nonperformance and liquidity are risks that market participants may consider under ASC 820. For an example illustrating how these risks may affect the fair value measurement, see ASC 820-10-55-90 through 55-98 (also see Section 10.6.4). Market participants may also consider other risks, including, but not limited to, model uncertainty risk and risks arising from the inability to hedge an underlying risk in an asset, liability, or instrument classified in an entity's stockholders' equity.

It may be difficult to determine a risk adjustment that a market participant would demand in an assumed transaction because the inputs in such a transaction might not be directly observable. In such situations, an entity should look beyond its own policies and transactions and consider the risks from a market participant's point of view.

When using Level 3 inputs, an entity may need to consider the following items, when applicable, to incorporate market participants' assumptions:

- Recent transactions of a similar nature and duration.
- Common industry practices.
- Historical trends and settlements of past transactions.

An entity may be able to calibrate its valuation technique to observed transaction prices to determine whether the risks that market participants would demand to be compensated for have been appropriately incorporated into the technique (see Section 10.3.3). See Section 10.6 for further discussion of adjustments that may be necessary when the volume or level of activity for an asset or liability has significantly decreased.

### 10.4.3 Premiums or Discounts Based on Size of a Position

#### 10.4.3.1 General

ASC 820-10-35-36B addresses when a fair value measurement should include a premium or discount as a result of the size of an asset, liability, or instrument classified in an entity's stockholders' equity. In a manner consistent with the guidance on transfer restrictions (see Section 10.2.2.2), a fair value measurement includes a premium or discount that reflects the size of the item only if size is a characteristic of the asset, liability, or instrument classified in stockholders’ equity. A fair value measurement cannot include “[p]remiums or discounts that reflect size as a characteristic of the . . . entity's holding” (i.e., a blockage factor) rather than as a characteristic of the asset, liability, or instrument classified in stockholders’ equity that is determined on the basis of its unit of account under other Codification topics (e.g., a control premium or minority interest discount that is appropriate on the basis of its unit of account). ASC 820-10-35-36B indicates that when “there is a quoted price in an active market . . . for an asset or a liability” (i.e., a Level 1 input), an entity must “use that quoted price without adjustment when measuring fair value, except as specified in paragraph 820-10-35-41C.” However, even if a fair value measurement is categorized within Level 2 or Level 3 of the fair value hierarchy in
its entirety, the fair value measurement cannot include a premium or discount for size (e.g., a blockage factor) when this premium or discount results from the size of an entity's holding rather than from a characteristic of the item being valued.

### 10.4.3.2 Unit of Account

The determination of whether size is a characteristic of an asset, liability, or instrument classified within an entity's stockholders' equity (and thus whether the fair value measurement should include a premium or discount for size) must be made on the basis of the unit of account for the item subject to the fair value measurement. The unit of account is generally determined under other Codification topics. See Chapter 4 for discussion of the unit of account.

ASC 820-10-35-44 addresses the unit of account for an asset or liability that is traded in an active market:

> If a reporting entity holds a position in a single asset or liability (including a position comprising a large number of identical assets or liabilities, such as a holding of financial instruments) and the asset or liability is traded in an active market, the fair value of the asset or liability shall be measured within Level 1 as the product of the quoted price for the individual asset or liability and the quantity held by the reporting entity. That is the case, even if a market's normal daily trading volume is not sufficient to absorb the quantity held and placing orders to sell the position in a single transaction might affect the quoted price.

The same “price times quantity” (or “P × Q”) approach must be applied in other situations for which the unit of account is an individual asset or liability. Thus, as discussed in Section 10.4.3.3 below, blockage factors are generally prohibited under ASC 820.

### 10.4.3.3 Blockage Factors

As described in ASC 820-10-35-36B, a blockage factor represents a discount that “adjusts the quoted price of an asset or a liability because the market's normal daily trading volume is not sufficient to absorb the quantity held by the entity.” The basic principle in ASC 820-10-35-36B is that blockage factors are prohibited at all levels of the fair value hierarchy. An adjustment to a quoted price of an individual asset or liability to reflect a blockage factor is not permitted under ASC 820 when the unit of account for the asset or liability is the individual instrument (i.e., the unit of account for the holding under U.S. GAAP is aligned with the unit of account related to the quoted price). For example, if an entity holds a large position in a publicly traded common stock and would expect to sell the position in a single transaction (i.e., a large block), the price it would receive would reflect a discount to the product of the quoted market price and the number of shares held; however, that discount should not be reflected in a fair value measurement because it reflects the size of the entity's holding as opposed to a characteristic of the asset held.

However, if the unit of account for fair value measurement purposes is the entire holding (i.e., entire position), an adjustment to reflect the size of the holding may be appropriate. Furthermore, if the unit of valuation reflects the entire holding, an adjustment to reflect the size of the holding may be appropriate even if the unit of account differs from the unit of valuation and application of a blockage factor at the unit-of-account level would be inappropriate. Thus, a discount that adjusts a quoted price of an asset or liability to reflect a blockage factor could, in certain circumstances, be consistent with the definition of fair value in ASC 820.

An entity would use a blockage factor (if market participants would incorporate one) when it applies the portfolio valuation exception in ASC 820-10-35-18D through 35-18L. ASC 820-10-35-18D permits an entity “to measure the fair value of a group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with Topic 815, or combinations of these items on the basis of the price that would be received to sell a net long position (that is, an asset) for a particular risk..."
exposure or paid to transfer a net short position (that is, a liability) for a particular risk exposure in an orderly transaction between market participants at the measurement date under current market conditions” (emphasis added). See Section 10.2.8.1 for more information about the portfolio valuation exception.

Examples 10-14 through 10-16 further illustrate the application of blockage factors in fair value measurements.

**Example 10-14**

**Bond Forward Contract — Blockage Factor Is Appropriate**

Entity M enters into a single-bond forward contract for the purchase of $1 billion in U.S. Treasury bonds. The contract is accounted for as a derivative instrument under ASC 815 and cannot be separated into denominations.

Quotes are available for futures contracts based on U.S. Treasury bonds that have a face value or notional amount of $100,000. Entity M might determine the fair value of its investment by multiplying the available quote by 10,000. However, this approach would not accurately reflect the characteristics of the contract, namely that the notional amount of M’s contract is $1 billion. According to ASC 820-10-35-36B, “[a] reporting entity [should] select inputs that are consistent with the characteristics of the asset or liability that market participants would take into account in a transaction for the asset or liability.” In this case, market participants would consider that, given the acquisition of the investment from M, a purchase of the entire contract would be required, of which the $1 billion notional amount is a characteristic.

Thus, it would be appropriate for M to adjust the observed $100,000 notional prices related to the bond forward contract for the size of its holding (i.e., one contract with a notional amount of $1 billion) because the size of the holding is a characteristic of the investment and both the unit of account and the unit of valuation are the $1 billion contract.

**Example 10-15**

**Bond Futures Contract — Blockage Factor Is Not Appropriate**

Entity N enters into 10,000 bond futures contracts, each with a notional amount of $100,000 (i.e., total notional amount of all contracts is $1 billion). The contracts are accounted for as derivative instruments under ASC 815. Quotes are available for futures contracts based on U.S. Treasury bonds that have a face value or notional amount of $100,000.

In this case, under ASC 820, N would not be permitted to consider its entire holding of 10,000 bond futures contracts as the unit of valuation in a fair value measurement because ASC 815 establishes the unit of account as each individual bond futures contract. Aggregating the bond futures contracts into a single unit of valuation would be inconsistent with ASC 820-10-35-36B. As a result, a blockage factor is not permitted. Rather, the fair value of N’s aggregate holding is equal to the quoted price of a single bond futures contract with a $100,000 notional amount multiplied by the 10,000 bond futures contracts held.

**Example 10-16**

**Application of the Portfolio Valuation Exception**

Entity O holds 15 long-term fixed-interest notes receivable with various counterparties. To manage its interest rate risk, O enters into 10 bond futures contracts. Information about its risk management strategies and related investments is provided to management. The notes receivable and futures contracts are both measured at fair value. Further, quoted prices are available for the bond futures contracts. However, O must use a combination of observable and unobservable inputs to determine the fair value for individual fixed-interest notes receivable. Entity O must first determine the unit of valuation to assess whether it may apply a discount that reflects size as a characteristic of its holding.
Example 10-16 (continued)

Generally, each individual note receivable, as well as each individual bond futures contract, represents a single unit of account and should be valued separately (i.e., the unit of valuation would be consistent with the unit of account). However, ASC 820-10-35-18D contains an exception to the ASC 820 measurement requirements regarding the unit of valuation. As discussed in Section 10.2.8.1, O must meet the following criteria in ASC 820-10-35-18E to apply this exception:

- It manages the group on the basis of the net exposure to interest rate risk in accordance with its documented risk management or investment strategy.
- It provides information on that basis about the group to the reporting entity’s management.
- It is required or has elected to measure the assets and liabilities in the group at fair value in the statement of financial position at the end of each reporting period.

In addition, O must consider whether the portfolio that consists of 15 notes receivable and 10 bond futures contracts achieves substantive offset. It would not be appropriate for O to apply the portfolio valuation exception in ASC 820-10-35-18D if the portfolio is not substantive. For example, a portfolio might not be substantive if it consisted of 15 notes receivable and one bond futures contract. In this example, without evidence to the contrary, it would appear that the portfolio was established to avoid the prohibition against blockage factors.

Entity O meets these criteria with respect to the 15 notes receivable and 10 bond futures contracts and measures the fair value of the portfolio on the basis of its net exposure (i.e., net asset basis). In this case, the net exposure is O’s unit of valuation for this fair value measurement even if prices are available for individual notes receivable and bond futures contracts. Thus, it would be appropriate for O to apply a discount that reflects size as a characteristic of its holding because size is a characteristic of the net exposure (the portfolio) that is being measured at fair value. Entity O should measure the fair value of the group in a manner consistent with how market participants would price the net risk exposure as of the measurement date.

10.4.3.4 Control Premiums

A control premium represents the amount a buyer is willing to pay for the synergies and other potential benefits that would be derived from controlling another entity. For example, incremental value could be associated with a controlling interest in a publicly traded company. The incremental value, or control premium, would represent the amount a buyer may be willing to pay in excess of the market capitalization of the publicly traded company (i.e., the product of the number of outstanding shares and the quoted price per share) to obtain a 100 percent ownership interest in that public company.

ASC 820-10-35-36B indicates that control premiums are not permitted as adjustments to Level 1 measurements. However, for other fair value measurements (i.e., Level 2 and 3 measurements), a control premium may be appropriate. For example, in fair value measurements of reporting units, a control premium may be relevant (see further discussion in Section 10.10.3.2). As another example, when the fair value of a noncontrolling interest is measured, a control premium and corresponding minority interest discount may be appropriate. Entities must evaluate relevant factors to determine whether a control premium is appropriate and, if so, must estimate the amount of the control premium.

See AICPA Technical Q&As Section 6910.35 for guidance on the inclusion of control premiums by investment companies when measuring the fair value of an investee.
10.4.4 Inputs Based on Bid and Ask Prices

Inputs Based on Bid and Ask Prices

35-36C If an asset or a liability measured at fair value has a bid price and an ask price (for example, an input from a dealer market), the price within the bid-ask spread that is most representative of fair value in the circumstances shall be used to measure fair value regardless of where the input is categorized within the fair value hierarchy (that is, Level 1, 2, or 3). The use of bid prices for asset positions and ask prices for liability positions is permitted but is not required.

35-36D This Topic does not preclude the use of mid-market pricing or other pricing conventions that are used by market participants as a practical expedient for fair value measurements within a bid-ask spread. For example, paragraphs 820-10-35-25 through 35-26 apply to a change from the use of mid-market pricing or other pricing conventions to another valuation technique. In addition, the disclosure requirements in paragraph 820-10-50-2(bbb) apply to such changes.

Pricing conventions are commonly used in certain industries. ASC 820-10-35-36C states that the “use of bid prices for asset positions and ask prices for liability positions is permitted but is not required.” Further, ASC 820-10-35-36D allows an entity to use “mid-market pricing or other pricing conventions that are used by market participants as a practical expedient for fair value measurements within a bid-ask spread.” An entity does not need to meet any qualifying criteria to use such conventions.

The decision to use such pricing as a practical expedient is an accounting policy election that should be consistently applied. It is generally inappropriate for an entity to change to using a practical expedient once it has established a policy of using the price that is most representative of fair value in the circumstances. For an entity to change its approach, the change must result in “a measurement that is equally or more representative of fair value in the circumstances” in accordance with ASC 820-10-35-25. Typically, such a change would not result in an equally or more representative measure of fair value.

In addition to establishing and consistently applying a policy for fair value measurements within a bid-ask spread, an entity should disclose its policy, if material.

The bid-ask spread practical expedient in ASC 820 is intended to be consistent with the SEC’s ASR 118, which states, in part:

Some companies as a matter of general policy use the bid price, others use the mean of the bid and asked prices, and still others use a valuation within the range considered best to represent the value in the circumstances; each of these policies is acceptable if consistently applied.

Example 10-17

Use of Pricing Convention Practical Expedient

Entity P and Broker-Dealer Y hold the same debt security. Broker-Dealer Y is a market maker in the debt security. Entity P is not a market maker in the debt security. Broker-dealers, including Y, trade the debt security in an active market by using the bid and ask prices. Entity P and Broker-Dealer Y’s respective policies are as follows:

- Although P would most likely sell the debt security at or close to the bid price, P may establish and consistently apply a policy of using the mid-market price as the fair value of the debt security (and other similar securities). However, in accordance with ASR 118, which states, “[n]ormally, it is not acceptable to use the asked price alone,” it would be inappropriate for P to use the ask price for its long position.
- Although Y may be able to exit at a price greater than the bid price, Y may have a consistently applied policy of carrying the same debt security (and other similar securities) by using the bid price.

See Section 9.2.1 for discussion of inception gains and losses.
10.4.5 Income Taxes

10.4.5.1 Income Tax Rate Used When an Income Approach Is Applied

When a fair value measurement is determined under an income approach on the basis of the present value of expected future cash flows, an entity may need to include an adjustment for income taxes. Such an adjustment would be most common in the valuation of nonfinancial assets or asset groups, such as a business, reporting unit, long-lived asset group, or intangible asset.

When income taxes are reflected in a fair value measurement by using an income approach, an entity would generally use the statutory rate unless there is substantial evidence that another tax rate should be used. Under ASC 820, fair value is determined from a market participant’s perspective. Therefore, entity-specific data, such as an entity’s own effective tax rate or the fact that the entity is not taxable (i.e., a partnership), are usually irrelevant. The above guidance is consistent with that in Chapter 6 of the AICPA Accounting and Valuation Guide Assets Acquired in a Business Combination to Be Used in Research and Development Activities, which states, in part:

> When choosing the appropriate tax rate, it is important to ensure that it does not reflect specific tax circumstances of the subject company, reporting entity, or both, which may occur by consideration of net operating loss carryforwards, tax penalties, special payments, and so forth. Instead, industry data demonstrating the tax rates experienced by market participants would need to be considered and compared with company-specific data and statutory rates.

The “tax rate experienced by market participants” would typically be the statutory income tax rate unless there is substantial evidence that another tax rate should be used.

10.4.5.2 Income Tax Benefits From Amortization of Intangible Assets

When an entity uses an income approach to measure the fair value of an intangible asset, the measurement should include tax benefits that a market participant would expect to receive for amortization expense that will be deducted on its tax return(s) in the future. That is, when using an income approach on a post-tax basis to measure the fair value of an intangible asset, an entity should include all incremental cash flows. These would include positive cash flows resulting from future income tax deductions for the asset’s amortization expense (commonly referred to as tax amortization benefits or “TABs”) that a market participant would expect to receive. A market participant would expect to receive the TABs if the jurisdiction in which the transaction is consummated allows for a deduction for amortization expense of intangible assets. An entity must use judgment in determining which jurisdiction should be considered from a market-participant perspective.

At the 2006 AICPA National Conference on Current SEC and PCAOB Developments, Cheryl Tjon-Hing, a valuation specialist in the SEC’s Office of the Chief Accountant, discussed how an entity should treat TABs in measuring an asset’s fair value. She stated, in part:

> Tax amortization benefits (TAB) represents, as its name implies, the cash flow generated to an owner of an asset as a result of being able to write-off the full fair value of that asset for tax purposes — generally, this benefit may impact a fair value conclusion, derived using an income approach, by as much as 20% to 30%. Now, it seems logical that the fair value of an asset should not change just because of the way a transaction is structured. So TABs should be taken into account, in determining asset fair values, no matter what the tax attributes of a transaction are. But for those requiring more specific guidance, FAS 109, paragraph A129 [footnote omitted] implicitly states that TABs should be factored into an asset’s fair value. To the extent that a portion of the step-up value is not deductible for tax purposes, that is what deferred tax liabilities are for. In fact, preparers of fair value measurements should be aware that if a TAB is not factored into the fair value of an asset, there may be a mismatch if any associated deferred tax liability is recorded, for accounting purposes, in an acquisition transaction. Now, despite the aforementioned accounting guidance, we often see that TABs are excluded from asset fair values measured for business combinations effected through a purchase of shares — usually, this is because preparers argue that any step-up in fair value over tax value is not deductible for tax purposes. [Emphasis added]
The AICPA Accounting and Valuation Guide *Assets Acquired in a Business Combination to Be Used in Research and Development Activities* includes a discussion of TABs and is a valuable resource for understanding and applying valuation techniques to intangible assets. See Section 10.1 for more information about the use of this practice aid.

### 10.4.6 Measuring the Fair Value of an Option

The term of an option that is measured at fair value under ASC 820 is one of the many inputs into a fair value measurement. Before determining whether it should use the expected term or the contractual term, an entity first needs to identify and select a valuation technique (or techniques) that is appropriate in the circumstances and for which sufficient data are available (see Section 10.3.2 for discussion of the use of multiple valuation techniques). The valuation technique should incorporate the inputs that market participants would consider when setting a price for the instrument.

If market participants would consider the contractual term in pricing the option, the entity's valuation technique also must incorporate the contractual term as an input, as might be the case, for example, with an option that can only be exercised at maturity and that is valued by using the Black-Scholes-Merton closed-form option pricing formula.

For options that may be terminated early, either upon early exercise or upon the occurrence of a contingent event (e.g., an IPO, a change in control, or a situation in which the share price exceeds a certain level), the entity may need to use a valuation technique that can incorporate dynamic assumptions about the term of the option. The fact that the term of the option is not fixed but depends on future conditions or events can be explicitly modeled. For example, an entity may use a binomial (lattice) model or simulation model that has been designed to reflect not only the option's contractual term but also early exercise behavior (e.g., as a function of the stock price level) or the likelihood that a contingency provision will be met at different points in time. Depending on the facts and circumstances, the Black-Scholes-Merton closed-form formula may not be an appropriate valuation technique for such an option, irrespective of whether the contractual term or the expected term is used as an input.

Entities should consider using a valuation specialist, as appropriate, and should document their process of selecting a valuation technique and its associated inputs, including their assumptions about the term used.

### 10.5 Fair Value Hierarchy

<table>
<thead>
<tr>
<th>ASC 820-10</th>
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<tbody>
<tr>
<td><strong>Fair Value Hierarchy</strong></td>
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<tr>
<td><strong>35-37</strong> To increase consistency and comparability in fair value measurements and related disclosures, this Topic establishes a fair value hierarchy that categorizes into three levels (see paragraphs 820-10-35-40 through 35-41, 820-10-35-41B through 35-41C, 820-10-35-44, 820-10-35-46 through 35-51, and 820-10-35-52 through 35-54A) the inputs to valuation techniques used to measure fair value. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1 inputs) and the lowest priority to unobservable inputs (Level 3 inputs).</td>
</tr>
<tr>
<td><strong>35-37A</strong> In some cases, the inputs used to measure the fair value of an asset or a liability might be categorized within different levels of the fair value hierarchy. In those cases, the fair value measurement is categorized in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement. Assessing the significance of a particular input to the entire measurement requires judgment, taking into account factors specific to the asset or liability. Adjustments to arrive at measurements based on fair value, such as costs to sell when measuring fair value less costs to sell, shall not be taken into account when determining the level of the fair value hierarchy within which a fair value measurement is categorized.</td>
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</table>
The availability of relevant inputs and their relative subjectivity might affect the selection of appropriate valuation techniques (see paragraph 820-10-35-24). However, the fair value hierarchy prioritizes the inputs to valuation techniques, not the valuation techniques used to measure fair value. For example, a fair value measurement developed using a present value technique might be categorized within Level 2 or Level 3, depending on the inputs that are significant to the entire measurement and the level of the fair value hierarchy within which those inputs are categorized.

If an observable input requires an adjustment using an unobservable input and that adjustment results in a significantly higher or lower fair value measurement, the resulting measurement would be categorized within Level 3 of the fair value hierarchy. For example, if a market participant would take into account the effect of a restriction on the sale of an asset when estimating the price for the asset, a reporting entity would adjust the quoted price to reflect the effect of that restriction. If that quoted price is a Level 2 input and the adjustment is an unobservable input that is significant to the entire measurement, the measurement would be categorized within Level 3 of the fair value hierarchy.

The FASB established the fair value hierarchy in Statement 157 (codified in ASC 820) to increase the consistency and comparability of fair value measurements and disclosures about such measurements. The hierarchy is divided into three categories on the basis of the relative observability and reliability of the inputs used in a fair value measurement. The categorization of inputs is important both to estimating fair value and to providing the related disclosures.

With respect to measuring fair value, the fair value hierarchy focuses on inputs rather than valuation techniques. However, ASC 820-10-35-38 indicates that the availability of inputs and their relative subjectivity might affect the selection of the valuation technique. For example, a valuation technique in which an entity uses relevant inputs classified within Level 2 of the fair value hierarchy takes precedence over a valuation technique containing significant unobservable inputs (i.e., Level 3 inputs). In addition, with limited exceptions, an entity is precluded from using a valuation technique that employs Level 2 or Level 3 inputs if a Level 1 quoted market price in an active market is available for an asset, liability, or equity instrument subject to fair value measurement.

ASC 820-10-35-37 through 35-38A give an overview of the fair value hierarchy, including the prioritization of inputs used in valuation techniques (which is relevant to the measurement of fair value) and the determination of the categorization of a fair value measurement in its entirety (which is relevant to disclosures about fair value measurements regardless of whether the item is measured or only disclosed at fair value). ASC 820-10-35-40 through 35-54D provide interpretive guidance on the categorization of inputs into the three levels of the fair value hierarchy. For more detailed discussion of the fair value hierarchy, see Chapter 8.
10.6 Measuring Fair Value When the Volume or Level of Activity for an Asset or Liability Has Significantly Decreased

10.6.1 General

| ASC 820-10 |

**Measuring Fair Value When the Volume or Level of Activity for an Asset or a Liability Has Significantly Decreased**

*35-54C* The fair value of an asset or a liability might be affected when there has been a significant decrease in the volume or level of activity for that asset or liability in relation to normal market activity for the asset or liability (or similar assets or liabilities). To determine whether, on the basis of the evidence available, there has been a significant decrease in the volume or level of activity for the asset or liability, a reporting entity shall evaluate the significance and relevance of factors such as the following:

a. There are few recent transactions.
b. Price quotations are not developed using current information.
c. Price quotations vary substantially either over time or among market makers (for example, some brokered markets).
d. Indices that previously were highly correlated with the fair values of the asset or liability are demonstrably uncorrelated with recent indications of fair value for that asset or liability.
e. There is a significant increase in implied liquidity risk premiums, yields, or performance indicators (such as delinquency rates or loss severities) for observed transactions or quoted prices when compared with the reporting entity's estimate of expected cash flows, taking into account all available market data about credit and other nonperformance risk for the asset or liability.
f. There is a wide bid-ask spread or significant increase in the bid-ask spread.
g. There is a significant decline in the activity of, or there is an absence of, a market for new issues (that is, a primary market) for the asset or liability or similar assets or liabilities.
h. Little information is publicly available (for example, for transactions that take place in a principal-to-principal market).

*35-54D* If a reporting entity concludes that there has been a significant decrease in the volume or level of activity for the asset or liability in relation to normal market activity for the asset or liability (or similar assets or liabilities), further analysis of the transactions or quoted prices is needed. A decrease in the volume or level of activity on its own may not indicate that a transaction price or quoted price does not represent fair value or that a transaction in that market is not orderly. However, if a reporting entity determines that a transaction or quoted price does not represent fair value (for example, there may be transactions that are not orderly), an adjustment to the transactions or quoted prices will be necessary if the reporting entity uses those prices as a basis for measuring fair value and that adjustment may be significant to the fair value measurement in its entirety. Adjustments also may be necessary in other circumstances (for example, when a price for a similar asset requires significant adjustment to make it comparable to the asset being measured or when the price is stale).

*35-54E* This Topic does not prescribe a methodology for making significant adjustments to transactions or quoted prices. See paragraphs 820-10-35-24 through 35-27 and 820-10-55-3A through 55-3G for a discussion of the use of valuation techniques when measuring fair value. Regardless of the valuation technique used, a reporting entity shall include appropriate risk adjustments, including a risk premium reflecting the amount that market participants would demand as compensation for the uncertainty inherent in the cash flows of an asset or a liability (see paragraph 820-10-55-8). Otherwise, the measurement does not faithfully represent fair value. In some cases, determining the appropriate risk adjustment might be difficult. However, the degree of difficulty alone is not a sufficient basis on which to exclude a risk adjustment. The risk adjustment shall be reflective of an orderly transaction between market participants at the measurement date under current market conditions.
Chapter 10 — Subsequent Measurement

ASC 820-10 (continued)

35-54F If there has been a significant decrease in the volume or level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate (for example, the use of a market approach and a present value technique). When weighting indications of fair value resulting from the use of multiple valuation techniques, a reporting entity shall consider the reasonableness of the range of fair value measurements. The objective is to determine the point within the range that is most representative of fair value under current market conditions. A wide range of fair value measurements may be an indication that further analysis is needed.

35-54G Even when there has been a significant decrease in the volume or level of activity for the asset or liability, the objective of a fair value measurement remains the same. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distress sale) between market participants at the measurement date under current market conditions.

35-54H Estimating the price at which market participants would be willing to enter into a transaction at the measurement date under current market conditions if there has been a significant decrease in the volume or level of activity for the asset or liability depends on the facts and circumstances at the measurement date and requires judgment. A reporting entity’s intention to hold the asset or to settle or otherwise fulfill the liability is not relevant when measuring fair value because fair value is a market-based measurement, not an entity-specific measurement.

ASC 820-10 — Glossary

Active Market
A market in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

ASC 820-10-35-54C through 35-54H contain guidance on the measurement of fair value when the volume or level of transactional activity for an asset or liability has significantly decreased. Note that even in these circumstances, the measurement must meet the objective in ASC 820-10-35-54G to be considered a fair value measurement. ASC 820-10-35-54G defines fair value as “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distress sale) between market participants at the measurement date under current market conditions.”

In addition to the discussion in the subsections that follow, see also Section 10.8 for discussion of the use of quotes from brokers or pricing services to measure the fair value of assets or liabilities for which the volume of transactional activity has significantly decreased.

10.6.2 Inactive Markets

10.6.2.1 Active Versus Inactive Markets

ASC 820-10-20 defines the term “active market,” and ASC 820-10-35-54C lists factors that may indicate that “there has been a significant decrease in the volume or level of activity . . . in relation to normal market activity for the asset or liability (or similar assets or liabilities).” An entity should evaluate these factors to determine whether their “significance and relevance” to the asset or liability are such that they result in an inactive market; however, the presence of one or more of these factors does not in itself mean that a market is not active. Further, a decline in the volume of transactions for a particular asset or

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12 This guidance, which amended Statement 157, was issued in 2009 in response to fair value measurement issues that arose during the credit crisis that began in 2007.
liability does not automatically make a market inactive. A market is inactive only when the frequency and volume of the transactions for the asset or liability are not sufficient to provide ongoing relevant pricing information. The characterization of a market as “active” or “inactive” may change as market conditions change.

In determining whether a market is active or inactive, an entity should focus on the trading activity of the individual asset or liability being measured rather than on the market in which it is traded. Therefore, a security that is traded infrequently on the NASDAQ could represent an asset that is not traded in an active market. However, a market is not deemed inactive simply because of insufficient trading volume relative to the size of an entity's position.

If an entity determines that a market is inactive, it must adhere to the fair value measurement objectives addressed in ASC 820-10-35-54G and 35-54H. Accordingly, the entity cannot use entity-specific assumptions instead of relevant observable market information in measuring fair value. See Section 10.6.3.2 for discussion of the impact on a fair value measurement of an entity's unwillingness to transact at current prices.

10.6.2.2 Distressed Sales Versus Inactive Markets

A low market demand for an asset (such as a debt security) may force prices down (i.e., supply-demand imbalances create pressure on market prices). However, in accordance with ASC 820-10-35-54I, in determining whether a transaction is orderly (and thus whether it meets the fair value objective described in ASC 820-10-35-54G), an entity cannot assume that an entire market is “distressed” (i.e., that all transactions in the market are forced or distressed transactions) and place less weight on observable transaction prices in measuring fair value. See Section 10.7 for more information about identifying transactions that are not orderly.

An entity must evaluate whether an observable transaction is not orderly (i.e., whether one of the parties is forced or otherwise compelled to transact) on a transaction-by-transaction basis, not on a market-wide basis. If orderly transactions are occurring between market participants in a manner that is usual and customary for transactions involving such assets, the entity can conclude that those transactions are not forced even if the market for such transactions is not active. An entity cannot, however, measure fair value by taking a “longer view” of the market in which the entity assumes that supply and demand will return to a reasonable balance.

In determining the price that would be received to sell an asset on the measurement date, an entity uses the assumptions that market participants would use, even if these assumptions differ from those the entity would use. For instance, if there is a quoted price in an active market for an identical asset, that quoted price generally provides the most reliable evidence of fair value and should be used to measure fair value even if the entity believes that the quoted price does not reflect long-term economic fundamentals. Alternatively, if there is no active market, the entity determines fair value by using a valuation technique (or multiple valuation techniques) that reflects current assumptions market participants would use, even if the assumptions differ from those that the entity would use in making decisions about transactions or for risk management purposes. Note that if the entity determines that the volume and level of activity for the asset have significantly decreased, transactions or quoted prices may not be determinative of fair value and the entity may be required to perform further analyses to determine whether transactions or quoted prices are orderly and whether a significant adjustment is necessary. If, after further analysis, the entity determines that the transactions are not orderly, it should place little to no weight on those transactions or quoted prices. See Section 10.7 for more information. See also Example 10-18 for an illustration.
10.6.3 Observable Transactions in Inactive Markets

10.6.3.1 General

Even if the market for an asset or liability is not active, observable transactions are relevant inputs to a fair value measurement when they reflect market participants' assumptions in orderly transactions. Under ASC 820, an entity prioritizes relevant observable inputs when measuring fair value. ASC 820-10-35-36 states that “[v]aluation techniques used to measure fair value shall maximize the use of relevant observable inputs and minimize the use of unobservable inputs.” Further, ASC 820-10-35-53 states, in part, that “[u]nobservable inputs [Level 3] shall be used to measure fair value to the extent that relevant observable inputs [Level 1 and 2] are not available.”

However, when the volume and level of activity have significantly decreased and the market is not active, observable transactions may not be representative of fair value. One possible reason for this is increased instances of transactions that are not orderly (e.g., forced liquidations or distress sales). Because the level of market activity does not affect the objective of a fair value measurement (i.e., the price in an orderly transaction between market participants as of the measurement date under current market conditions), an entity must further analyze the transactions or quoted prices under ASC 820-10-35-54D to determine whether they are orderly transactions representative of fair value. See Section 10.7 for more information about identifying transactions that are not orderly.

If an entity determines that a transaction is orderly, it should consider the transaction price when estimating fair value. However, the entity may also need to adjust those transactions when determining fair value. ASC 820-10-35-54J(b) states that the “amount of weight placed on that [orderly] transaction price when compared with other indications of fair value will depend on the facts and circumstances.”

If the entity determines that it does not need to significantly adjust the transaction price on the basis of unobservable inputs to arrive at the fair value of the asset or liability as of the measurement date, the transaction price represents a relevant observable input and the measurement would be classified as a Level 2 measurement. As discussed in Section 8.4.2.1, when an entity concludes that a single valuation technique results in superior information in terms of the fair value hierarchy (e.g., this technique results in a Level 2 measurement and alternative valuation techniques would result in Level 3 measurements), it should use that measurement technique to calculate fair value. However, if the entity must significantly adjust the transaction price on the basis of unobservable inputs, the measurement would be classified as a Level 3 measurement. In such circumstances, it may be appropriate for the entity to use multiple valuation techniques and weigh different indications of fair value to determine the amount that is most representative of fair value under current market conditions.

In some circumstances, a change in valuation technique or the use of multiple valuation techniques may be appropriate (e.g., the use of a market approach and a present value technique). For example, if an entity previously used quoted prices to determine fair value and there are no available quoted prices from orderly transactions, the entity may need to change its valuation technique or use multiple valuation techniques. If the entity determines fair value by using the transaction price from a disorderly transaction, adjusted to reflect the assumptions that market participants would use in pricing the asset or liability in an orderly transaction, the resulting measurement would generally be classified as a Level 3 measurement. See Section 10.3.4 for further discussion of changes in valuation techniques.
10.6.3.2 Unwillingness to Transact at Current Prices

As discussed in Section 7.1.4, market participants must be willing to enter into a transaction for the asset, liability, or equity instrument subject to the fair value measurement. They therefore must be motivated, but not forced or otherwise compelled, to enter into the transaction. An entity that owns an asset cannot merely disregard a price from an external source simply because the entity is not a “willing” seller at that price. ASC 820-10-35-54H indicates that an entity’s intention to hold an asset is not relevant to a fair value measurement, which is market-based and not entity-specific. If the best information available in the circumstances indicates that market participants would transact at the price from an external source, it does not matter whether the entity is willing to transact at that price.

See Section 10.6.3.3 below for discussion of adjustments to observable transaction prices. See also Example 10-19.

10.6.3.3 Adjustments to Observable Transaction Prices

The extent to which an entity can rely on a price obtained from an external source, and the potential adjustments necessary, depends on the facts and circumstances related to the price. The following are some considerations relevant to this evaluation:

- If the price is a quoted price (unadjusted) in an active market for an identical asset or liability, or for an identical liability when traded as an asset (i.e., it is a Level 1 input), the price should be used to determine fair value unless the exception in ASC 820-10-35-41C applies (see Section 8.2.1).

- If the price is the quoted price in an active market for a similar asset or liability, or for a similar liability when traded as an asset (i.e., it is a Level 2 input), the price generally serves as reliable evidence of fair value after the quoted price is adjusted for differences between the instrument being measured and the instrument underlying the quoted price (see Section 8.3.1.1).

- If there is no active market but the price is for an observed transaction as of the measurement date, the entity would need to assess whether that price reflects an orderly transaction. As discussed in Section 10.7, this evaluation would affect the significance or weight that the entity would assign to that price in measuring fair value. Note that, as discussed in ASC 820-10-35-54D, a decrease in the volume or level of activity on its own does not indicate that (1) a transaction price does not represent fair value or (2) the transaction was not orderly. However, if the entity determines that the observed transaction price does not reflect an orderly transaction, an adjustment to that price will be necessary if the entity uses that price as a basis for measuring fair value. In addition, if the observed transaction price is determined to represent an orderly market transaction but that transaction did not occur on the measurement date, adjustments to reflect differences in market conditions between the date of the transaction and the measurement date will also be necessary (i.e., to reflect fair value under current conditions as of the measurement date).

ASC 820-10-35-50 through 35-54M discuss when adjustments to Level 2 inputs may be appropriate (e.g., to reflect the volume and level of activity in the market in which the input is observed). A significant decline in volume and level of market activity may indicate that an entity needs to conduct further analysis to determine whether (1) the transaction or quoted price is determinative of fair value and (2) a significant adjustment to the transaction or quoted price may be necessary for the entity to measure the fair value in accordance with ASC 820.
• If a price is not based on observable market data (i.e., it is a Level 3 input), the entity may need to adjust the price or use a different valuation technique altogether to measure fair value. This may be the case if the price from the external source is not based on observable market data and the best available information in the circumstances suggests that the assumptions made by the external source differ from those a market participant would make in pricing the asset. ASC 820-10-35-54K states that in estimating fair value, an entity is not precluded from using “quoted prices provided by third parties, such as pricing services or brokers, if a reporting entity has determined that the quoted prices provided by those parties are developed in accordance with [ASC 820].” See Section 8.5 for further discussion of where prices from a broker or pricing service are categorized within the fair value hierarchy. See also Example 10-20.

In determining the types of adjustments that it may need to make to observed transaction prices, an entity may find it helpful to consider the guidance in the IASB Expert Advisory Panel report, which describes practices entities use when measuring the fair value of financial instruments. Paragraph 44 of this report states:

Factors that might lead to an adjustment to an observed transaction price for a similar instrument include (these might also be useful consideration in evaluating transactions in the same instrument):

(a) the timing of the transaction: if time has elapsed since the observed transaction, movements in market factors in the intervening period are considered and adjusted for.

(b) the terms of the instruments subject to the transaction: as economic and market conditions change, for example, market participants might require covenants for a new instrument that are different from those that were required for a previous instrument. This difference in terms affects the relative fair value of the two instruments. Furthermore, if a transaction contains complex terms and requires extensive documentation to explain the terms, market participants might demand a larger premium to compensate them for the effort required to understand and evaluate the terms of the specific instrument, or the potential additional hedging costs that might be incurred.

(c) any related transactions: for example, if a seller provides the finance for a sale to a buyer, and this finance is not at a market rate (and assuming there is no other transaction taking place), an adjustment is made to the transaction price to reflect the effect of the funding on that price.

(d) the correlation between the price of the instrument that is the subject of the observed transaction and the price of the instrument being measured: in general, the greater the correlation between the two instruments, the more relevant the observed transaction price is likely to be. When assessing correlations, it is important to remember that observed historical correlations cannot always be expected to continue, particularly if market conditions have changed.

In addition, if an entity uses a quoted price for a similar instrument in its valuation technique, the entity may need to make an adjustment to reflect differences in risk, including liquidity differences. For example, the instrument being measured may be in greater relative supply than a similar instrument for which a quoted price exists. In this situation, a liquidity risk difference would need to be factored into the fair value calculation as an adjustment to the quoted price of the other instrument.

An entity may also measure the fair value of a liability or instrument classified in its stockholders’ equity by using the quoted price of a similar but not identical item traded as an asset. In this case, the quoted price should be adjusted for factors specific to the asset that do not apply to the fair value measurement of the liability or equity instrument. ASC 820-10-35-16D indicates that an adjustment may be required when (1) the quoted price for the asset is related to a similar (but not identical) liability or equity instrument held by another party as an asset or (2) the unit of account for the asset is not the same as that for the liability or equity instrument. See Section 10.2.7 for further discussion.

See also Section 10.8.3 for discussion of the use of multiple quotes from brokers or pricing services.
10.6.4 Examples

**Example 10-18**

**Distressed Sale Versus Inactive Market**

Entity P holds an asset-backed debt security for which there is no active market. As a result of uncertainty about current and future prospects for the assets backing the security, there has been a sharp reduction in the number of potential investors for these securities in the market, increased price volatility, and a severe decline in liquidity. Investor demand for other similar debt securities has also decreased significantly. The decline in market demand forces prices down significantly, and risk premiums increase.

Entity P believes that the “true value” of the debt security is substantially higher than current observable transaction prices. In estimating the fair value of the debt security, P wants to take a “longer view” of the market under which supply and demand will return to a reasonable balance (sometimes known as “base value”). Such a view is premised on a conclusion that the entire market is “distressed.” Therefore, P plans to disregard current liquidity conditions and risk premiums in determining fair value.

In accordance with ASC 820, P is not permitted to determine fair value on the basis of a “longer view” of the market and cannot assume that an entire market is distressed. Rather, P should determine fair value by considering the price a willing market participant would pay for the debt security in an orderly transaction on the measurement date under current market conditions. Accordingly, P must evaluate whether any observable transactions, even if there are not very many, are orderly. Entity P is required to consider the impact that current market conditions, including illiquidity and imbalances in supply and demand (and the associated risk premiums), have on the price that would be received to sell the asset on the measurement date. Because a hypothetical transaction is assumed to be on the measurement date in a fair value measurement, it would generally be inappropriate for P to conclude that there are no willing buyers and no willing sellers.

**Example 10-19**

**Valuation of Debt Securities by Using Income Approach on the Basis of Observable Market Data**

Entity Q is using a valuation technique to determine the fair value of its holdings of privately placed corporate debt securities issued by Entity X. No quoted price for identical securities is available. Entity Q’s valuation technique takes into account assumptions about default rates and discount rates. Default rate assumptions can be readily derived from current observable market data for actively traded credit default swaps on X’s publicly traded bonds. In determining fair value, Q cannot disregard such market data even if it would not be willing to transact at a price consistent with the data. For a discussion of the use of internal data when market data exist, see Section 8.1.2.

**Example 10-20**

**Distressed Sale Versus Inactive Market**

Entity R holds distressed debt securities. There is no active market for the securities, but transactions occur infrequently and there are active markets for similar securities. Entity R’s own valuation model, which is based on observable Level 2 inputs current as of the measurement date, indicates that market participants would be willing to buy and sell the debt for $30 on the measurement date provided that marketing activities are usual and customary for transactions in similar securities. Entity R has calibrated the model by using the best information available as of the measurement date (including transaction prices related to comparable securities and risk premiums).

On the measurement date, a potential buyer provides an unsolicited bid to buy the securities for $20. While R cannot disregard the bid price simply because it is not willing to transact at that price, R cannot assume that the bid price serves as better evidence of fair value than its own model. The bid price is the price one potential buyer would be willing to pay for R’s asset but is not necessarily the price at which market participants (buyers and sellers) would be willing to transact on the measurement date.
Example 10-20 (continued)

ASC 820 requires that valuation techniques used to measure fair value maximize the use of relevant observable inputs (i.e., Level 1 and Level 2 inputs that do not require significant adjustment) and minimize the use of unobservable inputs (Level 3 inputs). If the bid price is classified as a Level 3 input and R's own model is based on Level 2 inputs, it may be appropriate for R to place less weight on the bid price in determining fair value. If R obtains several bid prices and the model amount is not in the range of prices obtained, however, it may be appropriate to challenge whether the model is valid and identify the reasons for the discrepancy.

If R's valuation technique involves obtaining prices periodically from potential buyers to determine fair value and validate the model amount, R should continue to apply this technique consistently unless a change would result in a measurement that is equally or more representative of fair value in the circumstances.

Example 8 in ASC 820-10-55-90 comprehensively illustrates how an entity measures fair value when the volume or level of activity for an asset or liability has significantly decreased:

**ASC 820-10**

**Example 8: Measuring Fair Value When the Volume or Level of Activity for an Asset or a Liability Has Significantly Decreased**

55-90 This Example illustrates the use of judgment when measuring the fair value of a financial asset when there has been a significant decrease in the volume or level of activity for the asset when compared with normal market activity for the asset (or similar assets). (See paragraphs 820-10-35-54C through 35-54H.) This Example has all of the following assumptions:

a. Entity A invests in a junior AAA-rated tranche of a residential mortgage-backed security on January 1, 20X8 (the issue date of the security).

b. The junior tranche is the third most senior of a total of seven tranches.

c. The underlying collateral for the residential mortgage-backed security is unguaranteed nonconforming residential mortgage loans that were issued in the second half of 20X6.

d. At March 31, 20X9 (the measurement date), the junior tranche is now A-rated. This tranche of the residential mortgage-backed security was previously traded through a brokered market. However, trading volume in that market was infrequent, with only a few transactions taking place per month from January 1, 20X8, to June 30, 20X8, and little, if any, trading activity during the nine months before March 31, 20X9.

55-91 Entity A takes into account the factors in paragraph 820-10-35-54C to determine whether there has been a significant decrease in the volume or level of activity for the junior tranche of the residential mortgage-backed security in which it has invested. After evaluating the significance and relevance of the factors, Entity A concludes that the volume and level of activity of the junior tranche of the residential mortgage-backed security have significantly decreased. Entity A supported its judgment primarily on the basis that there was little, if any, trading activity for an extended period before the measurement date.

55-92 Because there is little, if any, trading activity to support a valuation technique using a market approach, Entity A decides to use an income approach using the discount rate adjustment technique described beginning in paragraph 820-10-55-10 to measure the fair value of the residential mortgage-backed security at the measurement date. (See also paragraphs 820-10-35-36 through 35-36A.) Entity A uses the contractual cash flows from the residential mortgage-backed security. The discount rate adjustment technique described beginning in paragraph 820-10-55-10 would not be appropriate when determining whether there has been an other-than-temporary impairment and/or a change in yield in accordance with paragraph 325-40-35-4 when that technique uses contractual cash flows rather than most likely cash flows.
Because there is little, if any, trading activity to support a valuation technique using a market approach, Entity A decides to use an income approach using the discount rate adjustment technique described beginning in paragraph 820-10-55-10 to measure the fair value of the residential mortgage-backed security at the measurement date. (See also paragraphs 820-10-35-36 through 35-36A.) Entity A uses the contractual cash flows from the residential mortgage-backed security. The discount rate adjustment technique described beginning in paragraph 820-10-55-10 would not be appropriate when determining whether there has been a credit loss and/or a change in yield in accordance with paragraph 325-40-35-4 when that technique uses contractual cash flows rather than most likely cash flows.

Entity A then estimates a discount rate (that is, a market rate of return) to discount those contractual cash flows. The market rate of return is estimated using both of the following:

a. The risk-free rate of interest
b. Estimated adjustments for differences between the available market data and the junior tranche of the residential mortgage-backed security in which Entity A has invested. Those adjustments reflect available market data about expected nonperformance and other risks (for example, default risk, collateral value risk, and liquidity risk) that market participants would take into account when pricing the asset in an orderly transaction at the measurement date under current market conditions.

Entity A took into account the following information when estimating the adjustments in the preceding paragraph:

a. The credit spread for the junior tranche of the residential mortgage-backed security at the issue date as implied by the original transaction price
b. The change in credit spread implied by any observed transactions from the issue date to the measurement date for comparable residential mortgage-backed securities or on the basis of relevant indices
c. The characteristics of the junior tranche of the residential mortgage-backed security compared with comparable residential mortgage-backed securities or indices, including all of the following:
   1. The quality of the underlying assets, that is, information about all of the following:
      i. Delinquency rates
      ii. Foreclosure rates
      iii. Loss experience
      iv. Prepayment rates.
   2. The seniority or subordination of the residential mortgage-backed security tranche held
   3. Other relevant factors.
d. Relevant reports issued by analysts and rating agencies
e. Quoted prices from third parties such as brokers or pricing services.
Entity A estimates that one indication of the market rate of return that market participants would use when pricing the junior tranche of the residential mortgage-backed security is 12 percent (1,200 basis points). This market rate of return was estimated as follows:

a. Begin with 300 basis points for the relevant risk-free rate of interest at March 31, 20X9.

b. Add 250 basis points for the credit spread over the risk-free rate when the junior tranche was issued in January 20X8.

c. Add 700 basis points for the estimated change in the credit spread over the risk-free rate of the junior tranche between January 1, 20X8, and March 31, 20X9. This estimate was developed on the basis of the change in the most comparable index available for that time period.

d. Subtract 50 basis points (net) to adjust for differences between the index used to estimate the change in credit spreads and the junior tranche. The referenced index consists of subprime mortgage loans, whereas Entity A’s residential mortgage-backed security consists of similar mortgage loans with a more favorable credit profile (making it more attractive to market participants). However, the index does not reflect an appropriate liquidity risk premium for the junior tranche under current market conditions. Thus, the 50 basis point adjustment is the net of two adjustments.

1. The first adjustment is a 350 basis point subtraction, which was estimated by comparing the implied yield from the most recent transactions for the residential mortgage-backed security in June 20X8 with the implied yield in the index price on those same dates. There was no information available that indicated that the relationship between Entity A’s security and the index has changed.

2. The second adjustment is a 300 basis point addition, which is Entity A’s best estimate of the additional liquidity risk inherent in its security (a cash position) when compared with the index (a synthetic position). This estimate was derived after taking into account liquidity risk premiums implied in recent cash transactions for a range of similar securities.

As an additional indication of the market rate of return, Entity A also takes into account 2 recent indicative quotes (that is, nonbinding quotes) provided by reputable brokers for the junior tranche of the residential mortgage-backed security that imply yields of 15 to 17 percent. Entity A is unable to evaluate the valuation technique(s) or inputs used to develop the quotes. However, Entity A is able to confirm that the quotes do not reflect the results of transactions.

Because Entity A has multiple indications of the market rate of return that market participants would take into account when measuring fair value, it evaluates and weights the respective indications of the rate of return, considering the reasonableness of the range indicated by the results.

Entity A concludes that 13 percent is the point within the range of indications that is most representative of fair value under current market conditions. Entity A places more weight on the 12 percent indication (that is, its own estimate of the market rate of return) for the following reasons:

a. Entity A concluded that its own estimate appropriately incorporated the risks (for example, default risk, collateral value risk, and liquidity risk) that market participants would use when pricing the asset in an orderly transaction under current market conditions.

b. The broker quotes were nonbinding and did not reflect the results of transactions, and Entity A was unable to evaluate the valuation technique(s) or inputs used to develop the quotes.
10.7 Identifying Transactions That Are Not Orderly

10.7.1 General

**ASC 820-10**

**Identifying Transactions That Are Not Orderly**

35-54I The determination of whether a transaction is orderly (or is not orderly) is more difficult if there has been a significant decrease in the volume or level of activity for the asset or liability in relation to normal market activity for the asset or liability (or similar assets or liabilities). In such circumstances, it is not appropriate to conclude that all transactions in that market are not orderly (that is, forced liquidations or distress sales). Circumstances that may indicate that a transaction is not orderly include the following:

a. There was not adequate exposure to the market for a period before the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets or liabilities under current market conditions.

b. There was a usual and customary marketing period, but the seller marketed the asset or liability to a single market participant.

c. The seller is in or near bankruptcy or receivership (that is, the seller is distressed).

d. The seller was required to sell to meet regulatory or legal requirements (that is, the seller was forced).

e. The transaction price is an outlier when compared with other recent transactions for the same or a similar asset or liability.

A reporting entity shall evaluate the circumstances to determine whether, on the weight of the evidence available, the transaction is orderly.

35-54J A reporting entity shall consider all of the following when measuring fair value or estimating market risk premiums:

a. If the evidence indicates the transaction is not orderly, a reporting entity shall place little, if any, weight (compared with other indications of fair value) on that transaction price.

b. If the evidence indicates that a transaction is orderly, a reporting entity shall take into account that transaction price. The amount of weight placed on that transaction price when compared with other indications of fair value will depend on the facts and circumstances, such as the following:

1. The volume of the transaction
2. The comparability of the transaction to the asset or liability being measured
3. The proximity of the transaction to the measurement date.

c. If a reporting entity does not have sufficient information to conclude whether a transaction is orderly, it shall take into account the transaction price. However, that transaction price may not represent fair value (that is, the transaction price is not necessarily the sole or primary basis for measuring fair value or estimating market risk premiums). When a reporting entity does not have sufficient information to conclude whether particular transactions are orderly, the reporting entity shall place less weight on those transactions when compared with other transactions that are known to be orderly.

A reporting entity need not undertake exhaustive efforts to determine whether a transaction is orderly, but it shall not ignore information that is reasonably available. When a reporting entity is a party to a transaction, it is presumed to have sufficient information to conclude whether the transaction is orderly.

In an orderly transaction, there is a sufficient period of exposure to the market before the measurement date to allow for usual and customary marketing activities involving similar assets or liabilities. The length of the exposure period depends on the amount of time it takes market participants in typical transactions to agree on a transaction price for the type of asset or liability being measured.

For some assets (such as many financial instruments), the required period may elapse instantaneously or be measured in hours. For instance, no exposure may be required for an asset quoted in an active market (such as stock quoted on the NYSE) if current transaction prices are immediately available and
no additional marketing activities are required for a transaction to occur. Accordingly, ASC 820-10-35-41 generally requires that an entity use a quoted price in an active market to measure fair value whenever such a price is available, with limited exceptions. In addition, even if an active market does not exist for an identical instrument, the period of market exposure required for many types of financial instruments is often relatively short (e.g., when standard documentation exists and relevant observable market data are available to price the financial instrument). However, the period of market exposure for some types of financial instruments could be somewhat longer (e.g., a large portfolio of commercial loans that are measured by using significant unobservable inputs). In addition, a longer period of market exposure may be required for certain assets (e.g., servicing rights, real estate, or intangibles). In some markets, it is usual and customary for information dissemination, promotion, selling, and due diligence activities to take some time before a typical transaction can close.

While a period of exposure to the market is assumed in an orderly transaction, this does not mean that an entity can disregard changes in market conditions during that period or take a “longer view” of the market. Even when there is no observable market to provide pricing information about the sale of an asset or the transfer of a liability on the measurement date, in accordance with ASC 820-10-35-3, “[a] fair value measurement assumes that the asset or liability is exchanged in an orderly transaction between market participants to sell the asset or transfer the liability at the measurement date under current market conditions” (i.e., the fair value measurement objective). For instance, if the volume or level of activity in a market decreases because of a decline in investor demand, transaction prices in orderly transactions may also decrease. However, because those transaction prices are orderly, they are still relevant. In addition, if an entity uses a valuation technique to determine fair value, a decline in market liquidity might justify a higher risk premium or discount rate to reflect the increased risk inherent in the valuation technique or in the inputs to the valuation technique.

A transaction that is forced (e.g., a forced liquidation or distress sale) is not orderly. ASC 820-10-35-54J discusses the considerations an entity should take into account when the evidence indicates that a transaction is either (1) not orderly (in which case the entity should place little, if any, weight on the transaction price) or (2) orderly (in which case the entity must take the transaction price into account). ASC 820-10-35-54J also discusses the considerations related to situations in which an entity cannot conclude whether a transaction is orderly, in which case the entity must take the transaction price into account but place less weight on it than on other indications of fair value. In these situations, the transaction price cannot be the sole or primary basis for estimating fair value. Because the transaction price might not reflect the assumptions that market participants would use, it may be appropriate for the entity to use multiple valuation techniques and weigh different indications of fair value to determine the amount that is most representative of fair value under current market conditions.

13 Observable transactions as of or near the measurement date for an identical or similar asset or liability represent the most reliable evidence of the fair value of an asset or liability that is not transacted in an active market, provided that such transactions are orderly. However, an entity might need to make adjustments to such observable prices to reflect (1) differences between the item being measured at fair value and the asset or liability whose transaction price is observable or (2) changes in market conditions if the observable transaction is not as of or near the measurement date. If such adjustments are made on the basis of significant unobservable inputs, the fair value measurement in its entirety would be classified within Level 3 of the fair value hierarchy. In these circumstances, an entity may appropriately consider another valuation technique in measuring fair value. See also Section 10.6.3.3.
10.7.2 Determining Whether a Transaction Is Orderly

When measuring fair value, an entity assumes that the asset or liability is exchanged in an orderly transaction (i.e., not a forced liquidation or distress sale). Accordingly, an observable price based on transactions that are not orderly may not represent fair value. In measuring fair value, an entity may therefore need to adjust or place little, if any, weight on observable market data for transactions that are not orderly.

An entity evaluates whether a transaction is orderly on the basis of factors specific to the parties entering into the transaction (e.g., the seller’s financial difficulties). This evaluation is not based on general market conditions. For instance, it would not be appropriate to assume that a decline in an asset’s or liability’s volume or level of activity indicates that all sales or transfers of those assets or liabilities are not orderly. In other words, an entity cannot assume that an entire market is in “distress” (see Section 10.6.2.2). Thus, the entity should evaluate whether each transaction is orderly on the basis of the weight of the evidence available, as discussed in ASC 820-10-35-54I. In performing this evaluation, an entity will need to consider its specific facts and circumstances and may need to use significant judgment.

10.8 Using Quoted Prices by Third Parties

10.8.1 General

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**Using Quoted Prices Provided by Third Parties**

**35-54K** This Topic does not preclude the use of quoted prices provided by third parties, such as pricing services or brokers, if a reporting entity has determined that the quoted prices provided by those parties are developed in accordance with this Topic.

**35-54L** If there has been a significant decrease in the volume or level of activity for the asset or liability, a reporting entity shall evaluate whether the quoted prices provided by third parties are developed using current information that reflects orderly transactions or a valuation technique that reflects market participant assumptions (including assumptions about risk). In weighting a quoted price as an input to a fair value measurement, a reporting entity places less weight (when compared with other indications of fair value that reflect the results of transactions) on quotes that do not reflect the result of transactions.

**35-54M** Furthermore, the nature of a quote (for example, whether the quote is an indicative price or a binding offer) shall be taken into account when weighting the available evidence, with more weight given to quotes provided by third parties that represent binding offers.

Although entities may engage third-party advisers, such as pricing services or brokers, to help discharge management’s responsibilities, management must assume overall responsibility for determining both (1) the fair value of all assets, liabilities, or instruments classified within an entity’s stockholders’ equity that are measured at fair value and (2) the fair value measurement’s classification within the hierarchy. ASC 820-10-35-54K through 35-54M address management’s responsibilities related to using a pricing service or broker.

The requirement that management take responsibility for fair value measurements reported in the financial statements was also emphasized in a speech by Mark Shannon, associate chief accountant in the SEC’s Division of Corporation Finance, at the 2011 AICPA National Conference on Current SEC and PCAOB Developments. Mr. Shannon provided a sample of the types of comments that are typically issued to registrants that use third-party pricing information. The SEC staff in both the Division of
Corporation Finance and the Division of Investment Management asks similar questions of registrants and registered investment companies. Such questions address topics such as how the entity uses the pricing services in complying with financial statement accounting and disclosure requirements, MD&A disclosure, management’s assessment of ICFR, and the basic requirement to maintain books and records. Most notably, the staff has commented and asked questions about:

- Management’s evaluation of the appropriateness of the third-party models as well as the accuracy and completeness of the data used in the valuation.
- The assessment of the observability of the data used in the valuation and how the information affected the determination of the level within the fair value hierarchy.
- Third-party pricing service caveats regarding the use or reliability of the fair value estimates.
- The internal controls governing the use of the third-party pricing service.
- Management’s determination that assumptions used in the valuation are consistent with management’s accounting framework as well as with GAAP.

As indicated in ASC 820-10-35-54K and the SEC staff’s remarks, to take overall responsibility for determining fair value and the related disclosures when using a pricing service or broker, management will need to (1) understand whether the method the pricing service or broker uses to determine fair value is based on current information that reflects orderly transactions or a valuation technique that reflects market-participant assumptions (including assumptions about risks) and (2) assess the appropriateness of the values. On the basis of this understanding, management should determine the classification of the fair value measurement within the hierarchy. As noted in Section 8.5.1, an entity cannot assume that the pricing service or broker information is observable (i.e., Level 1 or Level 2) solely because the information comes from a third party. Rather, an entity needs to determine the proper classification within the fair value hierarchy as part of its process for determining that third-party information, such as broker quotes or pricing services, was developed in accordance with ASC 820. Management should also consider the implementation guidance in ASC 820-10-55-104(b), which suggests that in complying with the disclosure requirements in ASC 820, an entity might disclose “[h]ow third-party information such as broker quotes, pricing services, net asset values, and relevant market data was taken into account when measuring fair value.”

See Section 8.5 for further discussion of the classification within the fair value hierarchy of fair value measurements developed on the basis of pricing services or broker quotes.

### 10.8.2 When Broker or Pricing Service Quotes Represent Fair Value

ASC 820-10-35-54K indicates that an entity may use quoted prices provided by third parties, such as pricing services or brokers, provided that the entity has determined that those prices represent fair value under ASC 820. In addition, in a September 30, 2008, joint press release addressing ASC 820 application issues, the SEC’s Office of the Chief Accountant and the FASB staff indicated that “broker quotes may be an input when measuring fair value, but are not necessarily determinative if an active market does not exist for the security.”

In assessing whether a broker or pricing service quote is determinative of fair value, an entity needs to understand (1) how the broker or pricing service arrived at the quote and (2) the inputs or other information used. In a manner consistent with ASC 820-10-35-41, if a broker or pricing service quote represents the price quoted in an active market to which the entity has access, and the quote is for an identical asset, liability, or instrument classified in an entity’s stockholders’ equity, the entity is required to use this quote to determine fair value. Such a quote would represent a Level 1 input.
A broker or pricing service quote would not represent a Level 1 input in the absence of an active market or if a Level 1 input is adjusted in accordance with the criteria in ASC 820-10-35-41C. If the quote is not based on a Level 1 input but on a valuation technique that is used by market participants, reflects market-participant assumptions, and uses market-observable or market-corroborated inputs, the quote would be determinative of fair value provided that it does not need to be significantly adjusted. If a significant adjustment is needed, the quote is not determinative of fair value but could represent a relevant observable input into management’s determination of fair value.

The following are a few possible questions that entities should consider in evaluating whether a quote is determinative:

- Are there differences between the item being measured at fair value and the item for which a quote is available (e.g., differences in the terms or risk attributes)? Such differences may necessitate adjustments to the price quoted by the broker or pricing service.

- Does the quote reflect current orderly transactions for the item being measured? That is, are market participants currently transacting for the asset or liability at the price quoted by the broker or pricing service or does the quote reflect “stale” information or transactions that are not orderly? ASC 820-10-35-54L clarifies that an entity should place “less weight . . . on quotes that do not reflect the results of transactions.”

- Is the broker or pricing service using a valuation technique that complies with the fair value measurement principles in ASC 820? For example, does the valuation technique used by the broker or pricing service reflect market-participant assumptions, including assumptions about risk; maximize the use of relevant observable inputs; and minimize the use of unobservable inputs? If the valuation technique does not reflect the assumptions market participants would use in pricing the asset or liability, the price quoted by the broker or pricing service may not be relevant or may need to be adjusted.

- Is the quote provided by the broker or pricing service an indicative price or a binding offer? That is, does the broker or another market participant (or participants) stand ready to transact at the price quoted by the broker or pricing service? ASC 820-10-35-54M indicates that quotes based on binding offers should be weighted more heavily. Typically, a quote obtained from a broker or pricing service is an indicative price and not a binding offer (unless the broker is a market maker). If, however, a quote is a binding offer for an asset, the quote only definitively represents the “floor” for the fair value of the asset.

- Does the quote come from a reputable broker or pricing service that has a substantial presence in the market and the experience and expertise to provide a representationally faithful quote for the asset or liability being measured? An entity might place more weight on a quote from a broker or pricing service that has more experience and expertise related to the asset or liability being measured.

As the number of market transactions decreases, brokers or pricing services may rely more heavily on proprietary models to arrive at their quotes. An entity should determine how brokers or pricing services have arrived at their valuations as well as whether these valuations reflect market-participant assumptions (including assumptions about risk). This information may be difficult to obtain if quotes are based on proprietary models that brokers or pricing services might not be willing to share. However, although brokers or pricing services might not wish to share detailed information about their models, it might still be possible to obtain information about the nature of the assumptions and inputs used in the model (see Section 10.8.1 for more information about management’s responsibilities related to using third-party information to measure fair value). If the quote does not reflect assumptions that market participants would use in pricing the asset or liability, the quote may be a data point in the estimation of fair value but would most likely not be determinative since adjustments might be required. In addition,
other indications of fair value, such as a valuation based on management’s own estimates of the inputs that market participants would use in pricing the asset or liability, may be equally or more useful to an estimation of fair value.

An entity will need to perform additional analysis when quotes for an individual security are obtained from different brokers or pricing services. Multiple quotes within a narrow range constitute stronger evidence of fair value than multiple quotes that are widely dispersed. If an entity's own measurement of fair value is outside the range of broker or pricing service quotes, the entity should understand the cause(s) of such a difference. In addition, entities may find broker or pricing service quotes useful when calibrating their own models.

See Section 10.8.3 below for additional discussion of the evaluation an entity performs when multiple quotes are obtained. See Section 10.6 for discussion of considerations related to measuring fair value when the volume or level of activity for an asset or liability has significantly decreased.

10.8.3 Multiple Broker or Pricing Service Quotes

If an entity is using multiple quotes from brokers or pricing services to determine the fair value of a financial asset for which no active market exists (i.e., Level 2 or 3 inputs), the entity should consider the reasonableness of the range of quotes obtained regardless of whether the entity's purpose is to measure fair value or to calibrate its valuation technique. Using multiple sources may yield a wide range of quoted prices. If differences in quoted amounts are significant, it would be inappropriate to merely use an average of the quotes to determine fair value or calibrate a valuation technique.

As indicated in ASC 820-10-35-54F, if there are significant differences in the quoted amounts, the entity may need to further analyze the quotes. Further, paragraphs 55–57 of the IASB Expert Advisory Panel report note that when significant differences exist, an average does not represent a price at which a transaction would take place; it is likely that one of the quotes obtained better represents fair value than the other(s).

One possible cause of the discrepancy in pricing could be that different brokers or pricing services possess different amounts of information. For example, a broker that was involved in the original sale of an instrument might have information about that instrument that enables the broker to assess its fair value better than another broker or pricing service without that information. The more information an entity has about the basis for a quote, the easier it is to validate and rely on it.

If the volume and level of market activity for the asset or liability have significantly decreased and the market is not active, the entity should perform further analysis to determine whether the quotes are based on current information that reflects orderly transactions or a valuation technique that reflects market-participant assumptions (including assumptions about risk). In addition, ASC 820-10-35-54L states, in part, “[i]n weighting a quoted price as an input to a fair value measurement, a reporting entity places less weight (when compared with other indications of fair value that reflect the results of transactions) on quotes that do not reflect the result of transactions.” See Section 10.6 for more information about measuring fair value when the volume or level of activity for an asset or liability has significantly decreased.
10.9 Investments in Certain Entities That Calculate NAV per Share (or Its Equivalent)

<table>
<thead>
<tr>
<th>ASC 820-10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Measuring the Fair Value of Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)</strong></td>
</tr>
<tr>
<td><strong>35-59</strong> A reporting entity is permitted, as a practical expedient, to estimate the fair value of an investment within the scope of paragraphs 820-10-15-4 through 15-5 using the net asset value per share (or its equivalent, such as member units or an ownership interest in partners' capital to which a proportionate share of net assets is attributed) of the investment, if the net asset value per share of the investment (or its equivalent) is calculated in a manner consistent with the measurement principles of Topic 946 as of the reporting entity's measurement date.</td>
</tr>
<tr>
<td><strong>Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)</strong></td>
</tr>
<tr>
<td><strong>35-54B</strong> An investment within the scope of paragraphs 820-10-15-4 through 15-5 for which fair value is measured using net asset value per share (or its equivalent, for example member units or an ownership interest in partners' capital to which a proportionate share of net assets is attributed) as a practical expedient, as described in paragraph 820-10-35-59, shall not be categorized within the fair value hierarchy. In addition, the disclosure requirements in paragraph 820-10-50-2 do not apply to that investment. Disclosures required for an investment for which fair value is measured using net asset value per share (or its equivalent) as a practical expedient are described in paragraph 820-10-50-6A. Although the investment is not categorized within the fair value hierarchy, a reporting entity shall provide the amount measured using the net asset value per share (or its equivalent) practical expedient to permit reconciliation of the fair value of investments included in the fair value hierarchy to the line items presented in the statement of financial position in accordance with paragraph 820-10-50-2B.</td>
</tr>
</tbody>
</table>

ASC 820 allows entities, as a practical expedient, to measure the fair value of certain investments by using NAV per share (or its equivalent). When NAV per share (or its equivalent) is used to measure the fair value of an investment, the investment is not categorized within the fair value hierarchy and an entity does not need to provide certain disclosures that are otherwise required for assets measured at fair value on a recurring basis. See Section 2.2.2 for further discussion of the scope of this practical expedient. See Sections 11.2.2.3 and 11.3.2.3 for discussion of the disclosures an entity is required to provide when it uses this practical expedient.

10.10 Additional Fair Value Measurement Considerations

This section addresses the fair value measurement of specific types of assets, liabilities, or instruments classified in stockholders' equity that are covered in other Codification topics and that have not otherwise been discussed in this Roadmap.

10.10.1 Loan Receivables

10.10.1.1 General

Some entities, such as banks, mortgage banking entities, broker-dealers, and other financial services companies, recognize loan receivables (e.g., mortgage loans) at fair value through earnings in accordance with the FVO or specialized industry accounting practices. Entities that do not measure loan receivables at fair value may be required to disclose fair value amounts (see Sections 11.2.2.2 and 11.3.2.2).
An entity may estimate the fair value of a loan portfolio on the basis of one or more of the following approaches:

- Securitization pricing.
- Whole-loan pricing.
- Another income approach (e.g., a present value technique).

While entities may use different methods to measure the fair value of loans, paragraph BC46(a) of ASU 2011-04 states that “[t]he objective of a fair value measurement is to measure the asset that exists at the measurement date” (emphasis added). Entities should select their valuation method on the basis of the facts and circumstances. In accordance with ASC 820, in selecting the valuation method, an entity should consider (1) its principal (or most advantageous) market (see Chapter 6) and (2) the observability of relevant inputs. Regardless of the valuation technique(s) used, entities should consider calibration to (1) the transaction price if the transaction price equals fair value at initial recognition (see ASC 820-10-30-3A) and (2) prices received by the entity upon subsequent sales of loans. See Section 10.3.3 for further discussion of calibration.

The sections below discuss methods that may be used to determine the fair value of loans. See also Section 10.10.19.7.

### 10.10.1.2 Securitization Pricing

#### 10.10.1.2.1 General

Paragraph BC49 of ASU 2011-04 supports the use of securitization pricing and portfolio-level inputs:

> The Boards decided to clarify that although there are no excess returns available from holding financial assets and financial liabilities within a portfolio (because in an efficient market, the price reflects the benefits that market participants would derive from holding the asset or liability in a diversified portfolio), a fair value measurement assumes that market participants seek to maximize the fair value of a financial or nonfinancial asset or to minimize the fair value of a financial or nonfinancial liability by acting in their economic best interest in a transaction to sell the asset or to transfer the liability in the principal (or most advantageous) market for the asset or liability. Such a transaction might involve grouping assets and liabilities in a way in which market participants would enter into a transaction, if the unit of account specified in other Topics does not prohibit that grouping. [Emphasis added]

However, as discussed in Section 10.10.1.1, the objective of a fair value measurement is to measure the asset that exists as of the measurement date. Thus, while an entity could measure the fair value of a portfolio of loans on the basis of the sales proceeds that would be received in a hypothetical securitization, the objective is to arrive at a fair value measurement of the loans in their current condition and not the securities (beneficial interests in the loans) that may be issued in the future. Accordingly, a securitization price would need to be adjusted so that the price used to measure fair value reflects the current condition of the loans.

Use of an appropriately adjusted securitization price allows an entity to evaluate all inputs available and select the most reliable inputs (e.g., risk adjustments, the margin inherent in securitization, or the cost of guarantees or servicing). It is not appropriate for an entity to determine the fair value for a portfolio of loans by using a securitization price if the entity cannot make appropriate adjustments to the securitization price with the support of sufficient data.

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14 ASC 820-10-35-16A states that “[i]n all cases, a reporting entity [should] maximize the use of relevant observable inputs and minimize the use of unobservable inputs.” As a result, an entity is required to identify the most reliable (i.e., observable) inputs in determining the valuation technique(s) used to measure fair value. See further discussion in Section 10.3.
10.10.1.2.2 Additional Factors to Consider

As discussed in Section 10.10.1.2.1, an entity may measure the fair value of a loan portfolio on the basis of the estimated sales price of an executable securitization (i.e., securitization pricing), provided that the appropriate adjustments are made to the estimated securitization price. An entity that uses this approach to estimate the fair value of a loan portfolio is responsible for attaining relevant and reliable (i.e., observable) information to develop an appropriately adjusted securitization price.

An entity must evaluate estimated securitization prices to (1) understand whether they reflect orderly transactions in active markets for a portfolio of loans with characteristics that are identical or similar to the portfolio being valued, (2) make adjustments to account for differences between the quoted pool of loans and the portfolio of loans being valued, and (3) make other relevant adjustments as discussed below. In accordance with ASC 820, entities need to maximize the use of relevant observable inputs and minimize the use of unobservable inputs. When an entity uses a securitization price, it should understand and evaluate the source and reliability of inputs to prepare a fair value measurement for a portfolio of loans in their current form.

When using a securitization price to measure the fair value of a loan portfolio, an entity should consider the following:

- The securitization market must be the entity’s principal (or most advantageous) market — ASC 820-10-35-6 states, in part, that “[i]f there is a principal market for the asset or liability, the fair value measurement shall represent the price in that market (whether that price is directly observable or estimated using another valuation technique).” An entity’s principal market is the market that (1) the entity can access on the measurement date and (2) has the greatest volume or level of activity for the asset from a market participant’s perspective, which may be the securitization market. In the absence of a principal market, an entity should use the most advantageous market that it can access (in considering transaction costs, which are also further discussed below). See Chapter 6 for more information about the principal or most advantageous market.

- Entities that are new to the securitization market — An entity must have access to the securitization market for the securitization market to be the principal or most advantageous market; however, an entity does not need to have loans that are actually securitized to demonstrate such access. However, loan securitization involves many complex steps in which significant legal, underwriting, and other activities must be performed. Generally, the securitizer provides credit enhancement, usually by retaining certain beneficial interests. An entity that does not regularly securitize loans will need to provide evidence that a transaction is feasible and attainable. An entity that has not previously securitized loans would generally need evidence of significant progress toward effecting an actual securitization to demonstrate access to the securitization market.

- An entity needs to make appropriate adjustments when using a securitization price — Entities will need to adjust the securitization price for items that market participants would factor into the determination of fair value (because the portfolio of loans has not yet been transformed into securities). These items include the following:
  - Risk adjustments, including the effect of any uncertainty related to the ultimate securitization, model risk, or other risks.
  - Costs incurred to securitize the loan, whether transformation costs or transaction costs. Because the objective is to measure the portfolio of loans in their current condition, any costs related to accessing the securitization price should be incorporated into the fair value measurement of the whole-loan portfolio.
The cost of any guarantees (or other liabilities assumed) that the entity will provide (e.g., when a guarantee is contemplated as part of the securitization price used). One example of a guarantee is an early payment default or early prepayment provision. See Section 10.10.1.3.2 for additional information about such provisions.

Interests in the securitization that the entity may retain at their estimated current fair value, determined in accordance with ASC 820.

Other adjustments. According to ASC 820-10-30-3, the transaction price will often equal the exit price and therefore represents fair value at initial recognition. An entity should consider the conditions in ASC 820-10-30-3A to determine whether the fair value of a loan (or portfolio of loans) is equal to the transaction price at initial recognition. ASC 820-10-35-24C states that “[i]f the transaction price is fair value at initial recognition and a valuation technique that uses unobservable inputs will be used to measure fair value in subsequent periods [as may be the case for a valuation technique based on an appropriately adjusted securitization price], the valuation technique shall be calibrated so that at initial recognition the result of the valuation technique equals the transaction price.” Therefore, other adjustments to inputs used in a fair value measurement based on an appropriately adjusted securitization price are necessary if the fair value measurement would differ from the transaction price when the transaction price equals fair value at initial recognition. See Chapter 9 for further discussion of initial measurement.

The fair value measurement should be the price that would be received as of the measurement date; therefore, spot securitization prices should be used when available. An entity that uses forward prices should make adjustments to arrive at an estimate of the spot price on the measurement date. An appropriately adjusted securitization price would typically eliminate the margin or “gain” from the actual securitization.

Entities will need to determine a securitization price’s level within the fair value hierarchy by considering the lowest level of inputs significant to the measurement. One or more of the adjustments described above may be based on unobservable inputs. If these inputs are significant to the fair value measurement, they would cause the resulting fair value to be categorized within Level 3 of the fair value hierarchy.

10.10.1.3 Whole-Loan Pricing

10.10.1.3.1 General

In considering whether it is appropriate to measure the fair value of a portfolio of loans on the basis of whole-loan prices, an entity must consider whether:

- It has access to the whole-loan market.
- The whole-loan prices are identical or sufficiently similar to the loan portfolio being valued.
- The whole-loan prices reflect orderly transactions in an active market.
- Adjustments to observable whole-loan prices are necessary.

In evaluating whether whole-loan prices are identical or sufficiently similar to the loans being valued, an entity should consider whether it has retained or released servicing rights. Whole-loan prices may vary on the basis of whether servicing is retained or released, so an entity must ensure that it uses the correct price or make appropriate adjustments.
10.10.1.3.2 Additional Factors to Consider

Originators of certain loans (e.g., certain mortgage loans) have early payment default (EPD) and early prepayment agreements with purchasers (aggregators) of such whole loans. The purchaser pays a premium for these rights. These arrangements typically stipulate that if the obligor under the loan fails to make the initial payment on the loan (30 days or more past due) or prepays within a stipulated time frame (e.g., within 60 days of origination), the originator will repurchase the loan or refund the premium paid but the buyer will not incur a loss.

A portfolio of whole loans that is covered by such arrangements economically represents two elements: (1) a portfolio of whole loans and (2) short-term, contingent put (refund) rights under the EPD and early prepayment provisions. The rights under the EPD and early prepayment provisions are not characteristics of the loans since they are not part of the original loan agreements between the originator and the borrower.

These provisions are valuable to whole-loan buyers because loan sale transactions with these provisions command a higher price than those without the guarantee. The fair value of a portfolio of whole loans should not include any amounts related to the value of these provisions.

Entities will need to determine a whole-loan price’s level within the fair value hierarchy by considering the lowest level of inputs significant to the measurement. One or more adjustments to observable whole-loan prices may be based on unobservable inputs. If these inputs are significant to the fair value measurement, the resulting fair value would be categorized within Level 3 of the fair value hierarchy.

10.10.1.4 Present Value Technique

An entity that uses a discounted cash flow model would need to evaluate the reliability of inputs (e.g., prepayment and default assumptions) that are used to develop projected cash flows. In addition, the entity should evaluate the source and reliability of the information used to develop an appropriate discount rate on the basis of the risk profile, prepayment and default rates, and other characteristics of the portfolio being valued.

10.10.2 Equity Securities

Fair value measurements of investments in equity securities without readily determinable fair values will represent Level 2 or Level 3 measurements (or measurements on the basis of NAV per share). Either a market approach or an income approach will be used in such fair value measurements. In preparing such measurements, an entity may find it useful to consult the AICPA Accounting and Valuation Guide Valuation of Privately-Held-Company Equity Securities Issued as Compensation. See also Sections 9.2 and 10.10.19.3.

As discussed in Section 2.3.2.1.2, when the measurement alternative in ASC 321-10-35-2 is applied to an investment in an equity security that does not have a readily determinable fair value, the measurement adjustment that is recognized upon a remeasurement event (i.e., an impairment or observable price change in an identical or similar investment of the same issuer) represents a fair value measurement under ASC 820. An entity is also required to comply with the nonrecurring disclosure requirements in ASC 820 when such a remeasurement event occurs.

A fair value measurement used to recognize an impairment on an equity security for which the measurement alternative in ASC 321-10-35-2 is applied may be estimated on the basis of either a market approach or income approach. Entities must consider the lowest-level significant input used in the valuation technique to determine the appropriate classification of the measurement within the fair value hierarchy (see Chapter 8 for more information).
A fair value measurement used to recognize an observable price change for an equity security to which the measurement alternative in ASC 321-10-35-2 is applied will be based on either an observable transaction in an identical security or a similar investment of the same issuer. Paragraph BC112 of ASU 2019-04 addresses how to measure the fair value change under ASC 321-10-35-2 that arises from an observable price involving the identical or similar security:

The Board believed that, in most cases, the observable price change in an orderly transaction of the identical or similar investment of the same issuer would generally represent the fair value change in that investment. The Board intended a consistent remeasurement at fair value for investments accounted for under the measurement alternative upon identifying (a) an orderly transaction of the identical or similar investment of the same issuer, (b) an orderly transaction of a similar investment of the same issuer, and (c) impairment. Therefore, the Board intended to require a nonrecurring fair value measurement in accordance with Topic 820 upon the occurrence and identification of any remeasurement event described in Topic 321 for equity securities without readily determinable fair value accounted for under the measurement alternative.

If the equity investment is remeasured on the basis of the observable price change without adjustment, this nonrecurring fair value measurement would represent a Level 1 or Level 2 fair value measurement. However, if unobservable inputs are used to make significant adjustments to the observable price, the nonrecurring fair value measurement would be classified within Level 3 of the fair value hierarchy.

10.10.3 Reporting Units

10.10.3.1 General

**ASC 350-20**

**Determining the Fair Value of a Reporting Unit**

35-22 The fair value of a reporting unit refers to the price that would be received to sell the unit as a whole in an orderly transaction between market participants at the measurement date. Quoted market prices in active markets are the best evidence of fair value and shall be used as the basis for the measurement, if available. However, the market price of an individual equity security (and thus the market capitalization of a reporting unit with publicly traded equity securities) may not be representative of the fair value of the reporting unit as a whole.

35-23 Substantial value may arise from the ability to take advantage of synergies and other benefits that flow from control over another entity. Consequently, measuring the fair value of a collection of assets and liabilities that operate together in a controlled entity is different from measuring the fair value of that entity's individual equity securities. An acquiring entity often is willing to pay more for equity securities that give it a controlling interest than an investor would pay for a number of equity securities representing less than a controlling interest. That control premium may cause the fair value of a reporting unit to exceed its market capitalization. The quoted market price of an individual equity security, therefore, need not be the sole measurement basis of the fair value of a reporting unit.

35-24 In estimating the fair value of a reporting unit, a valuation technique based on multiples of earnings or revenue or a similar performance measure may be used if that technique is consistent with the objective of measuring fair value. Use of multiples of earnings or revenue in determining the fair value of a reporting unit may be appropriate, for example, when the fair value of an entity that has comparable operations and economic characteristics is observable and the relevant multiples of the comparable entity are known. Conversely, use of multiples would not be appropriate in situations in which the operations or activities of an entity for which the multiples are known are not of a comparable nature, scope, or size as the reporting unit for which fair value is being estimated.
### Deferred Income Tax Considerations

**35-25** Before estimating the fair value of a reporting unit, an entity shall determine whether that estimation should be based on an assumption that the reporting unit could be bought or sold in a nontaxable transaction or a taxable transaction. Making that determination is a matter of judgment that depends on the relevant facts and circumstances and must be evaluated carefully on a case-by-case basis (see Examples 1 through 2 [paragraphs 350-20-55-10 through 55-23]).

### Pending Content (Transition Guidance: ASC 350-20-65-3)

**35-25** Before estimating the fair value of a reporting unit, an entity shall determine whether that estimation should be based on an assumption that the reporting unit could be bought or sold in a nontaxable transaction or a taxable transaction. Making that determination is a matter of judgment that depends on the relevant facts and circumstances and must be evaluated carefully on a case-by-case basis (see Example 1 [paragraphs 350-20-55-10 through 55-23]).

### 10.10.3.2 Impact of Control Premium on Measuring the Fair Value of a Reporting Unit

When the fair value of a reporting unit is measured by reference to quoted market prices of that reporting unit's individual equity securities, the presence of a control premium must be evaluated and, if deemed appropriate, factored into the fair value measurement.

The concept of a control premium is addressed in ASC 350-20-35-22 and 35-23, which state, in part:

> [T]he market price of an individual equity security (and thus the market capitalization of a reporting unit with publicly traded equity securities) may not be representative of the fair value of the reporting unit as a whole.

Substantial value may arise from the ability to take advantage of synergies and other benefits that flow from control over another entity. Consequently, measuring the fair value of a collection of assets and liabilities that operate together in a controlled entity is different from measuring the fair value of that entity's individual equity securities. An acquiring entity often is willing to pay more for equity securities that give it a controlling interest than an investor would pay for a number of equity securities representing less than a controlling interest. That control premium may cause the fair value of a reporting unit to exceed its market capitalization. The quoted market price of an individual equity security, therefore, need not be the sole measurement basis of the fair value of a reporting unit.

Under ASC 350-20-35-22 and 35-23, when measuring the fair value of a reporting unit by referring to the quoted market price of the reporting unit's individual equity securities (price multiplied by quantity), an entity may need to adjust the measurement for a control premium. An adjustment for the control
premium, if deemed applicable, lowers the fair value measurement below Level 1. ASC 820-10-55-21(h) and ASC 820-10-55-22(e) give examples of Level 2 and Level 3 inputs, respectively, for a reporting unit. In addition, if individual reporting units do not have separately traded equity securities, it would be inappropriate to allocate the per-share market value of the consolidated entity’s equity to the individual reporting units.

In a speech at the 2008 AICPA National Conference on Current SEC and PCAOB Developments, Robert G. Fox III addressed the SEC staff's view on determining the reasonableness of control premiums:

[T]he amount of a control premium in excess of a registrant's market capitalization can require a great deal of judgment. Contrary to some rumors I have heard, the staff does not have “bright line” tests that we use in determining the reasonableness of a control premium. Instead, we believe that a registrant needs to carefully analyze the facts and circumstances of their particular situation when determining an appropriate control premium and that there is normally a range of reasonable judgments a registrant might reach. While it would be prudent to reconcile the combined fair value of your reporting units to your market capitalization, I believe that this should not be viewed as the only factor to consider in assessing goodwill for impairment.

See Section 10.4.3.4 for further discussion of control premiums.

10.10.3.3 Determining Fair Value When an Entity Has Only One Reporting Unit

Even if an entity has only one reporting unit, it may not be appropriate to measure the fair value of that reporting unit solely on the basis of a quoted market price in an active market. While ASC 350-20-35-22 states that “[q]outed market prices in active markets are the best evidence of fair value,” it also notes that these market prices may not represent fair value as a whole. Therefore, in certain instances in which an entity has only one reporting unit, the current quoted market price of the entity's publicly traded securities may not represent the entity's fair value. For example, a market participant may be willing to pay a premium over the current market price to obtain the synergies and other benefits that control would provide (i.e., a control premium). Such a control premium is appropriate when the unit of account is the reporting unit. See Section 10.10.3.2 for discussion of the incorporation of a control premium into the fair value of a reporting unit.

10.10.3.4 Equity Value Versus Enterprise Value

ASC 350 does not require entities to use an equity value or enterprise value when calculating the fair value of a reporting unit to evaluate the unit for impairment or recognize an impairment loss. This conclusion is consistent with paragraph BC26 of ASU 2017-04, which states:

GAAP does not prescribe the valuation premise that an entity must use in the impairment test. It only mandates that the same assets and liabilities be used to determine both the carrying amount and fair value and that the methodology be consistently applied.

Further, paragraph BC4 of ASU 2010-28 states, in part:

The Task Force evaluated the different approaches used to calculate the carrying amount of reporting units. Some Task Force members thought choosing an approach for calculating the carrying amount of a reporting unit was an accounting principle choice, while others thought it was a choice of estimation methods. One Task Force member was concerned that this diversity would effectively allow a publicly traded single reporting unit to look to something other than its quoted market price as evidence of fair value. The Task Force decided to address the concerns about diversity in practice without mandating an approach for calculating the carrying amount of a reporting unit for purposes of Step 1 of the goodwill impairment test, even for entities with single reporting units. The Task Force observed that the manner in which the fair value and carrying amount of the reporting unit is determined should be consistent. [Emphasis added]

In addition, in a speech at the 2009 AICPA National Conference on Current SEC and PCAOB Developments, SEC staff member Evan Sussholz discussed whether the fair value of a reporting unit refers to the unit's equity value or enterprise value. He stated that enterprise value is “commonly defined
as the sum of the fair value of debt and equity” and further indicated that the SEC staff would not expect
the results of a goodwill impairment assessment to be affected if an entity uses equity value instead of
enterprise value.

10.10.3.5 Changing the Method of Determining the Fair Value of a Reporting Unit

Although ASC 350-20 provides guidance on determining the fair value of a reporting unit, it does not
indicate whether the same method must be used every time an entity performs the goodwill impairment
test. While the method entities use to calculate the fair value of a reporting unit should generally be
consistent, a different method may yield more reliable results in certain instances. For example, instead
of or in addition to using a present value technique, a reporting unit that completes a public offering of
its common stock may wish to measure the stock’s fair value by using a market approach in which the
stock’s quoted market price is used as an input. However, entities should not change their methods to
avoid recognizing, or accelerate the recording of, a goodwill impairment charge.

10.10.4 Intangible Assets

As discussed in Section 10.3.1, the three widely used valuation techniques are the market approach,
cost approach, and income approach. It is generally not appropriate to use the market approach in
measuring the fair value of a customer-relationship intangible asset because, in such circumstances,
there may be an absence of market transactions involving identical or comparable assets. Use of the
cost approach also may not be appropriate in such cases, as indicated in a speech by SEC staff member
Chad A. Kokenge at the 2003 AICPA National Conference on Current SEC Developments:

[T]he [cost] approach only focuses on the entity’s specific costs that are necessary to “establish” the
relationship. Such an approach would not be sensitive to the volume of business that might be generated by
the customer, other relationship aspects, such as referral capability, or other factors that may be important to
how a marketplace participant might assess the asset. If these factors are significant, we believe the use of such
an approach would generally be inconsistent with the . . . definition of fair value.

Accordingly, the income approach will generally be used to measure the fair value of a customer-
relationship intangible asset. However, in applying the income approach, an entity should also consider
the following prepared remarks made by SEC staff member Joseph B. Ucuzoglu at the 2006 AICPA
National Conference on Current SEC and PCAOB Developments:

Some have suggested that the SEC staff always requires the use of an income approach to value customer
relationship intangible assets. The staff has even heard some suggest that, as long as a registrant characterizes
its valuation method as an income approach, the specific assumptions used or results obtained will not be
challenged by the staff, because one has complied with a perceived bright line requirement to use an income
approach. Let me assure you, these statements are simply false. While an income approach often provides the
most appropriate valuation of acquired customer relationship intangible assets, circumstances may certainly
indicate that a different method provides a better estimate of fair value. On the flipside, even when a registrant
concludes that an income approach is the most appropriate valuation methodology, the staff may nevertheless
question the result obtained when the underlying assumptions, such as contributory asset charges, do not
appear reasonable in light of the circumstances.

When determining the appropriate valuation of a customer relationship intangible asset, I believe that the first
step in the process should be to obtain a thorough understanding of the value drivers in the acquired entity.
That is, why is it that customers continually return to purchase products or services from the acquired entity?
In some cases, the nature of the relationship may be such that customers are naturally “sticky,” and tend
to stay with the same vendor over time without frequently reconsidering their purchasing decisions. In that
circumstance, it would appear that a significant portion of the ongoing cash flows that the acquired entity will
generate can be attributed to the strength of its customer relationships.

At the other end of the spectrum, relationships may be a less significant value driver in an environment where
customers frequently reassess their purchasing decisions and can easily switch to another vendor with a
lower price or a superior product. In that environment, if customers continually return to buy products from
the acquired entity, perhaps they do so in large part due to factors other than the relationship, such as a
well-known tradename, strong brands, and proprietary technologies. As a result, the value of the customer relationship intangible asset may be less than would be the case in a circumstance where the relationship is stronger. However, the staff would generally expect that the amount attributed to other intangible assets would be commensurately higher, reflecting the increasingly important role of those assets in generating cash flows.

10.10.5 Internal-Use Software

<table>
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<th>ASC 350-40</th>
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<tbody>
<tr>
<td>Impairment</td>
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<tr>
<td>35-3 When it is no longer probable that computer software being developed will be completed and placed in service, the asset shall be reported at the lower of the carrying amount or fair value, if any, less costs to sell. The rebuttable presumption is that such uncompleted software has a fair value of zero. Indications that the software may no longer be expected to be completed and placed in service include the following:</td>
</tr>
<tr>
<td>a. A lack of expenditures budgeted or incurred for the project.</td>
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<tr>
<td>b. Programming difficulties that cannot be resolved on a timely basis.</td>
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<tr>
<td>c. Significant cost overruns.</td>
</tr>
<tr>
<td>d. Information has been obtained indicating that the costs of internally developed software will significantly exceed the cost of comparable third-party software or software products, so that management intends to obtain the third-party software or software products instead of completing the internally developed software.</td>
</tr>
<tr>
<td>e. Technologies are introduced in the marketplace, so that management intends to obtain the third-party software or software products instead of completing the internally developed software.</td>
</tr>
<tr>
<td>f. Business segment or unit to which the software relates is unprofitable or has been or will be discontinued.</td>
</tr>
</tbody>
</table>

If an entity ceases development of software and there is reliable evidence that the project can be marketed in its present state, the related capitalized cost balance should be reported in accordance with ASC 360-10-35 at the lower of the carrying amount or fair value less costs to sell. In all cases, as noted in ASC 350-40-35-3, there is a rebuttable presumption that an uncompleted software project “has a fair value of zero.”

If an entity continues development because it has decided to market the software to others, the entity should apply the guidance in ASC 985-20, regardless of whether it is probable that the software will be completed and placed in service by the entity itself. ASC 350-40-35-9 requires that the carrying amount be evaluated as of each balance sheet date in accordance with ASC 985-20-35-4.
10.10.6 PP&E

**ASC 360-10**

*Fair Value*

35-36 For long-lived assets (asset groups) that have uncertainties both in timing and amount, an expected present value technique will often be the appropriate technique with which to estimate fair value.

*Measurement of Expected Disposal Loss or Gain*

35-38 Costs to sell are the incremental direct costs to transact a sale, that is, the costs that result directly from and are essential to a sale transaction and that would not have been incurred by the entity had the decision to sell not been made. Those costs include broker commissions, legal and title transfer fees, and closing costs that must be incurred before legal title can be transferred. Those costs exclude expected future losses associated with the operations of a long-lived asset (disposal group) while it is classified as held for sale. Expected future operating losses that marketplace participants would not similarly consider in their estimates of the fair value less cost to sell of a long-lived asset (disposal group) classified as held for sale shall not be indirectly recognized as part of an expected loss on the sale by reducing the carrying amount of the asset (disposal group) to an amount less than its current fair value less cost to sell. If the sale is expected to occur beyond one year as permitted in limited situations by paragraph 360-10-45-11, the cost to sell shall be discounted.

*Long-Lived Assets to Be Abandoned*

35-48 Because the continued use of a long-lived asset demonstrates the presence of service potential, only in unusual situations would the fair value of a long-lived asset to be abandoned be zero while it is being used. When a long-lived asset ceases to be used, the carrying amount of the asset should equal its salvage value, if any. The salvage value of the asset shall not be reduced to an amount less than zero.

*Management Expects to Sell Asset and Remediation Costs Not Required*

55-11 Management expects to sell the asset in the future, and the asset's sale will not require the environmental remediation costs to be incurred. (Although the environmental remediation costs are excluded from this Subtopic's recoverability test, the fair value of the asset is likely to be affected by the existence of those costs. The diminished fair value shall be considered in estimating the cash flows expected to arise from the eventual sale of the asset.)

*Case B: Expected Cash Flows Technique*

55-30 This Case illustrates the application of an expected present value technique to estimate the fair value of a long-lived asset in an impairment situation.
The following table shows by year the computation of the expected cash flows used in the measurement. They reflect the possible cash flows (probability-weighted) used to test the manufacturing facility for recoverability in Case A, adjusted for relevant marketplace assumptions, which increases the possible cash flows in total by approximately 15 percent.

<table>
<thead>
<tr>
<th>Year</th>
<th>Possible Cash Flows (Market) (in $ millions)</th>
<th>Probability Assessment</th>
<th>Expected Cash Flows (Undiscounted) (in $ millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>$4.6</td>
<td>20%</td>
<td>$0.9</td>
</tr>
<tr>
<td></td>
<td>$6.3</td>
<td>50</td>
<td>$3.2</td>
</tr>
<tr>
<td></td>
<td>$7.5</td>
<td>30</td>
<td>$2.3</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>$6.4</td>
</tr>
<tr>
<td>2</td>
<td>$4.6</td>
<td>20%</td>
<td>$0.9</td>
</tr>
<tr>
<td></td>
<td>$6.3</td>
<td>50</td>
<td>$3.2</td>
</tr>
<tr>
<td></td>
<td>$7.5</td>
<td>30</td>
<td>$2.3</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>$6.4</td>
</tr>
<tr>
<td>3</td>
<td>$4.3</td>
<td>20%</td>
<td>$0.9</td>
</tr>
<tr>
<td></td>
<td>$5.8</td>
<td>50</td>
<td>$2.9</td>
</tr>
<tr>
<td></td>
<td>$6.7</td>
<td>30</td>
<td>$2.0</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>$5.8</td>
</tr>
<tr>
<td>4</td>
<td>$4.3</td>
<td>20%</td>
<td>$0.9</td>
</tr>
<tr>
<td></td>
<td>$5.8</td>
<td>50</td>
<td>$2.9</td>
</tr>
<tr>
<td></td>
<td>$6.7</td>
<td>30</td>
<td>$2.0</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td>$5.8</td>
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<tr>
<td>5</td>
<td>$4.0</td>
<td>20%</td>
<td>$0.8</td>
</tr>
<tr>
<td></td>
<td>$5.4</td>
<td>50</td>
<td>$2.7</td>
</tr>
<tr>
<td></td>
<td>$6.4</td>
<td>30</td>
<td>$1.9</td>
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<td>$5.4</td>
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<tr>
<td>6</td>
<td>$4.0</td>
<td>20%</td>
<td>$0.8</td>
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<tr>
<td></td>
<td>$5.4</td>
<td>50</td>
<td>$2.7</td>
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<tr>
<td></td>
<td>$6.4</td>
<td>30</td>
<td>$1.9</td>
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<td></td>
<td>$5.4</td>
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<tr>
<td>7</td>
<td>$3.9</td>
<td>20%</td>
<td>$0.8</td>
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<tr>
<td></td>
<td>$5.1</td>
<td>50</td>
<td>$2.6</td>
</tr>
<tr>
<td></td>
<td>$5.6</td>
<td>30</td>
<td>$1.7</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td>$5.1</td>
</tr>
<tr>
<td>8</td>
<td>$3.9</td>
<td>20%</td>
<td>$0.8</td>
</tr>
<tr>
<td></td>
<td>$5.1</td>
<td>50</td>
<td>$2.6</td>
</tr>
<tr>
<td></td>
<td>$5.6</td>
<td>30</td>
<td>$1.7</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td>$5.1</td>
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<tr>
<td>9</td>
<td>$3.9</td>
<td>20%</td>
<td>$0.8</td>
</tr>
<tr>
<td></td>
<td>$5.0</td>
<td>50</td>
<td>$2.5</td>
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<tr>
<td></td>
<td>$5.5</td>
<td>30</td>
<td>$1.7</td>
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<tr>
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<td></td>
<td></td>
<td>$5.0</td>
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<tr>
<td>10</td>
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<td>20%</td>
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<tr>
<td></td>
<td>$6.0</td>
<td>50</td>
<td>$3.0</td>
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<td></td>
<td>$6.5</td>
<td>30</td>
<td>$2.0</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td>$6.0</td>
</tr>
</tbody>
</table>
The following table shows the computation of the expected present value; that is, the sum of the present values of the expected cash flows by year, each discounted at a risk-free interest rate determined from the yield curve for U.S. Treasury instruments. In this case, a market risk premium is included in the expected cash flows; that is, the cash flows are certain equivalent cash flows. As shown, the expected present value is $42.3 million, which is less than the carrying amount of $48 million. In accordance with paragraph 360-10-35-17 the entity would recognize an impairment loss of $5.7 million.

<table>
<thead>
<tr>
<th>Year</th>
<th>Expected Cash Flows (Undiscounted) (in $ millions)</th>
<th>Probability Assessment</th>
<th>Expected Present Value (in $ millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>$ 6.4</td>
<td>5.0%</td>
<td>$ 6.1</td>
</tr>
<tr>
<td>2</td>
<td>6.4</td>
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<td>5.8</td>
</tr>
<tr>
<td>3</td>
<td>5.8</td>
<td>5.2</td>
<td>5.0</td>
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<tr>
<td>4</td>
<td>5.8</td>
<td>5.4</td>
<td>4.7</td>
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<tr>
<td>5</td>
<td>5.4</td>
<td>5.6</td>
<td>4.1</td>
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<tr>
<td>6</td>
<td>5.4</td>
<td>5.8</td>
<td>3.9</td>
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<tr>
<td>7</td>
<td>5.1</td>
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<td>3.4</td>
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<tr>
<td>8</td>
<td>5.1</td>
<td>6.2</td>
<td>3.2</td>
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<tr>
<td>9</td>
<td>5.0</td>
<td>6.4</td>
<td>2.9</td>
</tr>
<tr>
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<td>6.0</td>
<td>6.6</td>
<td>3.2</td>
</tr>
<tr>
<td></td>
<td>$ 56.4</td>
<td></td>
<td>$ 42.3</td>
</tr>
</tbody>
</table>

See Section 2.3.7 for more information about the testing of long-lived assets for impairment.

10.10.7 Asset Retirement and Environmental Obligations

ASC 410-20

Fair Value Is Reasonably Estimated

25-6 An entity shall identify all its asset retirement obligations. An entity has sufficient information to reasonably estimate the fair value of an asset retirement obligation if any of the following conditions exist:

a. It is evident that the fair value of the obligation is embodied in the acquisition price of the asset.

b. An active market exists for the transfer of the obligation.

c. Sufficient information exists to apply an expected present value technique.

Obligations With Uncertainty in Timing or Method of Settlement

25-7 The obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and (or) method of settlement. Thus, the timing and (or) method of settlement may be conditional on a future event. Accordingly, an entity shall recognize a liability for the fair value of a conditional asset retirement obligation if the fair value of the liability can be reasonably estimated. In some cases, sufficient information about the timing and (or) method of settlement may not be available to reasonably estimate fair value. An expected present value technique incorporates uncertainty about the timing and method of settlement into the fair value measurement. Uncertainty is factored into the measurement of the fair value of the liability through assignment of probabilities to cash flows.
An entity would have sufficient information to apply an expected present value technique and therefore an asset retirement obligation would be reasonably estimable if either of the following conditions exists:

a. The settlement date and method of settlement for the obligation have been specified by others. For example, the law, regulation, or contract that gives rise to the legal obligation specifies the settlement date and method of settlement. In this situation, the settlement date and method of settlement are known and therefore the only uncertainty is whether the obligation will be enforced (that is, whether performance will be required). In certain cases, determining the settlement date for the obligation that has been specified by others is a matter of judgment that depends on the relevant facts and circumstances. For example, a contract that provides the entity with an ability to extend its term through renewal should be evaluated to determine whether the settlement date should take into consideration renewal periods. Uncertainty about whether performance will be required does not defer the recognition of an asset retirement obligation because a legal obligation to stand ready to perform the retirement activities still exists, and it does not prevent the determination of a reasonable estimate of fair value because the only uncertainty is whether performance will be required.

b. The information is available to reasonably estimate all of the following:
   1. The settlement date or the range of potential settlement dates
   2. The method of settlement or potential methods of settlement (The term potential methods of settlement refers to methods of settling the obligation that are currently available to the entity. Therefore, uncertainty about future methods yet to be developed would not prevent the entity from estimating the fair value of the asset retirement obligation.)
   3. The probabilities associated with the potential settlement dates and potential methods of settlement. (The entity should have a reasonable basis for assigning probabilities to the potential settlement dates and potential methods of settlement to reasonably estimate the fair value of the asset retirement obligation. If the entity does not have a reasonable basis of assigning probabilities, it is expected that the entity would still be able to reasonably estimate fair value when the range of time over which the entity may settle the obligation is so narrow and (or) the cash flows associated with each potential method of settlement are so similar that assigning probabilities without having a reasonable basis for doing so would not have a material impact on the fair value of the asset retirement obligation.)

In many cases, the determination as to whether the entity has the information to reasonably estimate the fair value of the asset retirement obligation is a matter of judgment that depends on the relevant facts and circumstances. It is expected that the narrower the range of time over which the entity may settle the obligation and the fewer potential methods of settlement the entity has available to it, the more likely it is that the entity will have the information to reasonably estimate the fair value of an asset retirement obligation. For an illustration of this guidance, see Example 3 (paragraph 410-20-55-47).

Instances may occur in which sufficient information to estimate the fair value of an asset retirement obligation is unavailable. For example, if an asset has an indeterminate useful life, sufficient information to estimate a range of potential settlement dates for the obligation might not be available. In such cases, the liability would be initially recognized in the period in which sufficient information exists to estimate a range of potential settlement dates that is needed to employ a present value technique to estimate fair value.

Examples of information that is expected to provide a basis for estimating the potential settlement dates, potential methods of settlement, and the associated probabilities include, but are not limited to, information that is derived from the entity's past practice, industry practice, management's intent, or the asset's estimated economic life. The estimated economic life of the asset might indicate a potential settlement date for the asset retirement obligation. However, the original estimated economic life of the asset may not, in and of itself, establish that date because the entity may intend to make improvements to the asset that could extend the life of the asset or the entity could defer settlement of the obligation beyond the economic life of the asset. In those situations, the entity would look beyond the economic life of the asset in determining the settlement date or range of potential settlement dates to use when estimating the fair value of the asset retirement obligation.
Uncertainty in Performance Obligations

25-15 An unambiguous requirement that gives rise to an asset retirement obligation coupled with a low likelihood of required performance still requires recognition of a liability. Uncertainty about the conditional outcome of the obligation is incorporated into the measurement of the fair value of that liability, not the recognition decision. Uncertainty about performance of conditional obligations shall not prevent the determination of a reasonable estimate of fair value. A past history of nonenforcement of an unambiguous obligation does not defer recognition of a liability, but its measurement is affected by the uncertainty over the requirement to perform retirement activities.

Determination of a Reasonable Estimate of Fair Value

30-1 An expected present value technique will usually be the only appropriate technique with which to estimate the fair value of a liability for an asset retirement obligation. An entity, when using that technique, shall discount the expected cash flows using a credit-adjusted risk-free rate. Thus, the effect of an entity's credit standing is reflected in the discount rate rather than in the expected cash flows. Proper application of a discount rate adjustment technique entails analysis of at least two liabilities—the liability that exists in the marketplace and has an observable interest rate and the liability being measured. The appropriate rate of interest for the cash flows being measured shall be inferred from the observable rate of interest of some other liability, and to draw that inference the characteristics of the cash flows shall be similar to those of the liability being measured. Rarely, if ever, would there be an observable rate of interest for a liability that has cash flows similar to an asset retirement obligation being measured. In addition, an asset retirement obligation usually will have uncertainties in both timing and amount. In that circumstance, employing a discount rate adjustment technique, where uncertainty is incorporated into the rate, will be difficult, if not impossible. See paragraphs 410-20-55-13 through 55-17 and Example 2 (paragraph 410-20-55-35). For further information on present value techniques, see the guidance beginning in paragraph 820-10-55-4.

Allocation of Asset Retirement Cost

35-6 The subsequent measurement provisions require an entity to identify undiscounted estimated cash flows associated with the initial measurement of a liability. Therefore, an entity that obtains an initial measurement of fair value from a market price or from a technique other than an expected present value technique must determine the undiscounted cash flows and estimated timing of those cash flows that are embodied in that fair value amount for purposes of applying the subsequent measurement provisions. Example 1 (see paragraph 410-20-55-31) provides an illustration of the subsequent measurement of a liability that is initially obtained from a market price. (See paragraph 410-20-25-14 for a discussion on conditional outcomes.)

35-7 Paragraph 410-20-25-14 explains how uncertainty surrounding conditional performance of a retirement obligation is factored into its measurement by assessing the likelihood that performance will be required. As the time for notification approaches, more information and a better perspective about the ultimate outcome will likely be obtained. Consequently, reassessment of the timing, amount, and probabilities associated with the expected cash flows may change the amount of the liability recognized. See paragraphs 410-20-55-18 through 55-19.

Components of a Larger System

55-11 If assets with asset retirement obligations are components of a larger group of assets (for example, a number of oil wells that make up an entire oil field operation), aggregation techniques may be necessary to derive a collective asset retirement obligation. This Subtopic does not preclude the use of estimates and computational shortcuts that are consistent with the fair value measurement objective when computing an aggregate asset retirement obligation for assets that are components of a larger group of assets. This implementation guidance illustrates paragraph 410-20-30-1.
This implementation guidance illustrates Section 410-20-15. If, for example, a governmental unit retains the right (an option) to decide whether to require a retirement activity, there is some uncertainty about whether those retirement activities will be required or waived. Regardless of the uncertainty attributable to the option, a legal obligation to stand ready to perform retirement activities still exists, and the governmental unit might require them to be performed. Although the timing and method of settlement of the retirement obligation may depend on future events that may or may not be within the control of the entity, a legal obligation to stand ready to perform retirement activities still exists. The entity should consider the uncertainty about the timing and method of settlement in the measurement of the liability, consistent with a fair value measurement objective, regardless of whether the event that will trigger the settlement is partially or wholly under the control of the entity.

Expected Present Value Technique

This implementation guidance illustrates paragraph 410-20-30-1. In estimating the fair value of a liability for an asset retirement obligation using an expected present value technique, an entity shall begin by estimating the expected cash flows that reflect, to the extent possible, a marketplace assessment of the cost and timing of performing the required retirement activities. Considerations in estimating those expected cash flows include developing and incorporating explicit assumptions, to the extent possible, about all of the following:

a. The costs that a third party would incur in performing the tasks necessary to retire the asset
b. Other amounts that a third party would include in determining the price of the transfer, including, for example, inflation, overhead, equipment charges, profit margin, and advances in technology
c. The extent to which the amount of a third party's costs or the timing of its costs would vary under different future scenarios and the relative probabilities of those scenarios
d. The price that a third party would demand and could expect to receive for bearing the uncertainties and unforeseeable circumstances inherent in the obligation, sometimes referred to as a market-risk premium.

It is expected that uncertainties about the amount and timing of future cash flows can be accommodated by using the expected present value technique and therefore will not prevent the determination of a reasonable estimate of fair value.

Credit-Adjusted Risk-Free Rate

This implementation guidance illustrates paragraph 410-20-30-1. An entity shall discount expected cash flows using an interest rate that equates to a risk-free interest rate adjusted for the effect of its credit standing (a credit-adjusted risk-free rate). In determining the adjustment for the effect of its credit standing, an entity should consider the effects of all terms, collateral, and existing guarantees on the fair value of the liability.

Adjustments for default risk can be reflected in either the discount rate or the expected cash flows. In most situations, an entity will know the adjustment required to the risk-free interest rate to reflect its credit standing. Consequently, it would be easier and less complex to reflect that adjustment in the discount rate.

In addition, because of the requirements in paragraph 410-20-35-8 relating to upward and downward adjustments in expected cash flows, it is essential to the operationality of this Subtopic that the credit standing of the entity be reflected in the discount rate. For those reasons, the risk-free rate shall be adjusted for the credit standing of the entity to determine the discount rate.
Historical Waste on Electrical and Electronic Equipment Associated With EU Directive 2002/96/EC

55-27 If the asset is subsequently replaced, with the obligation being transferred to the producer of the replacement equipment, the commercial user should determine the portion of the total amount paid to the producer that relates to the replacement equipment (the new asset) and the portion that relates to the transfer of the asset retirement obligation. That determination should be based on the fair value of the asset retirement obligation, without the sale of the new asset. The price paid by the commercial user would not include any costs associated with the transfer of the obligation in situations in which the law in the EU-member country obligates commercial users to pay all of the costs associated with the historical waste even if the equipment is replaced. In those situations, the commercial user would not derecognize the liability from its balance sheet upon replacement, but rather when the obligation is ultimately settled.

ASC 410-20-55-31 through 55-67 contain several examples illustrating fair value estimates. See Section 10.2.7.5 for an example from ASC 820 that illustrates the application of the guidance in ASC 420-10 to an ARO liability. For further discussion of fair value estimates related to AROs, see also Deloitte’s A Roadmap to Accounting for Environmental Obligations and Asset Retirement Obligations.

10.10.8 Exit or Disposal Cost Obligations

10.10.8.1 General

ASC 420-10

Fair Value

30-1 A liability for a cost associated with an exit or disposal activity shall be measured initially at its fair value in the period in which the liability is incurred, except as indicated in paragraphs 420-10-30-4 and 420-10-30-6 (for a liability for one-time termination benefits that is incurred over time).

30-2 Quoted market prices are the best representation of fair value. However, for many of the liabilities covered by this Subtopic, quoted market prices will not be available. Consequently, in those circumstances, fair value will be estimated using some other valuation technique. A present value technique is often the best available valuation technique with which to estimate the fair value of a liability for a cost associated with an exit or disposal activity. For a liability that has uncertainties both in timing and amount, an expected present value technique generally will be the appropriate technique.

30-3 In some situations, a fair value measurement for a liability associated with an exit or disposal activity obtained using a valuation technique other than a present value technique may not be materially different from a fair value measurement obtained using a present value technique. In those situations, this Subtopic does not preclude the use of estimates and computational shortcuts that are consistent with a fair value measurement objective.

Contract Termination Costs

30-8 If the contract is an operating lease, the fair value of the liability at the cease-use date shall be determined based on the remaining lease rentals, adjusted for the effects of any prepaid or deferred items recognized under the lease, and reduced by estimated sublease rentals that could be reasonably obtained for the property, even if the entity does not intend to enter into a sublease. Remaining lease rentals shall not be reduced to an amount less than zero.

Pending Content (Transition Guidance: ASC 842-10-65-1)

30-8 Paragraph superseded by Accounting Standards Update No. 2016-02.
Example 1: One-Time Employee Termination Benefits — No Future Service Required

55-2 This Example assumes that an entity has a one-time benefit arrangement established by a plan of termination that meets the criteria in paragraph 420-10-25-4 and has been communicated to employees.

55-3 An entity plans to cease operations in a particular location and determines that it no longer needs the 100 employees that currently work in that location. The entity notifies the employees that they will be terminated in 90 days. Each employee will receive as a termination benefit a cash payment of $6,000, which will be paid at the date an employee ceases rendering service during the 90-day period. In accordance with paragraph 420-10-25-8, a liability would be recognized at the communication date and, in accordance with paragraph 420-10-30-5, measured at its fair value. In this case, because of the short discount period, $600,000 may not be materially different from the fair value of the liability at the communication date.

Example 2: One-Time Employee Termination Benefits — Stay Bonus—Future Service Required

55-4 This Example assumes that an entity has a one-time benefit arrangement established by a plan of termination that meets the criteria in paragraph 420-10-25-4 and has been communicated to employees.

55-5 An entity plans to shut down a manufacturing facility in 16 months and, at that time, terminate all of the remaining employees at the facility. To induce employees to stay until the facility is shut down, the entity establishes a one-time stay bonus arrangement. Each employee that stays and renders service for the full 16-month period will receive as a termination benefit a cash payment of $10,000, which will be paid 6 months after the termination date. An employee that leaves voluntarily before the facility is shut down will not be entitled to receive any portion of the termination benefit. In accordance with paragraph 420-10-25-9, a liability for the termination benefits would be measured initially at the communication date and, in accordance with paragraph 420-10-30-6, based on the fair value of the liability as of the termination date and recognized ratably over the future service period. The fair value of the liability as of the termination date would be adjusted cumulatively for changes resulting from revisions to estimated cash flows over the future service period, measured using the credit-adjusted risk-free rate that was used to measure the liability initially (as illustrated in this Example).

55-6 The fair value of the liability as of the termination date is $962,240, estimated at the communication date using an expected present value technique. The expected cash flows of $1 million (to be paid 6 months after the termination date), which consider the likelihood that some employees will leave voluntarily before the facility is shut down, are discounted for 6 months at the credit-adjusted risk-free rate of 8 percent. In this case, a risk premium is not considered in the present value measurement. Because the amounts of the cash flows will be fixed and certain as of the termination date, marketplace participants would not demand a risk premium.

55-7 Therefore, a liability of $60,140 would be recognized in each month during the future service period (16 months).

55-8 After eight months, more employees than originally estimated leave voluntarily. The entity adjusts the fair value of the liability as of the termination date to $769,792 to reflect the revised expected cash flows of $800,000 (to be paid 6 months after the termination date), discounted for 6 months at the credit-adjusted risk-free rate that was used to measure the liability initially (8 percent). Based on that revised estimate, a liability (expense) of $48,112 would have been recognized in each month during the future service period. Thus, the liability recognized to date of $481,120 ($60,140 × 8) would be reduced to $384,896 ($48,112 × 8) to reflect the cumulative effect of that change (of $96,224). A liability of $48,112 would be recognized in each month during the remaining future service period (8 months). Accretion expense would be recognized after the termination date in accordance with the guidance beginning in paragraph 420-10-35-1 and in paragraph 420-10-45-5.

Example 3: One-Time Employee Termination Benefits — Voluntary and Involuntary Benefits Offered

55-9 This Example assumes that an entity has a one-time benefit arrangement established by a plan of termination that meets the criteria of paragraph 420-10-25-4 and has been communicated to employees.
**ASC 420-10 (continued)**

55-10 An entity initiates changes to streamline operations in a particular location and determines that, as a result, it no longer needs 100 of the employees that currently work in that location. The plan of termination provides for both voluntary and involuntary termination benefits (in the form of cash payments). Specifically, the entity offers each employee (up to 100 employees) that voluntarily terminates within 30 days a voluntary termination benefit of $10,000 to be paid at the separation date. Each employee that is involuntarily terminated thereafter (to reach the target of 100) will receive an involuntary termination benefit of $6,000 to be paid at the termination date. The entity expects all 100 employees to leave (voluntarily or involuntarily) within the minimum retention period. In accordance with paragraphs 420-10-25-6 through 25-8, a liability for the involuntary termination benefit (of $6,000 per employee) would be recognized at the communication date and, in accordance with paragraphs 420-10-30-4 through 30-6, measured at its fair value. In this case, because of the short discount period, $600,000 may not be materially different from the fair value of the liability at the communication date. As noted in paragraph 420-10-25-10, a liability for the incremental voluntary termination benefit (of $4,000 per employee) would be recognized in accordance with paragraph 712-10-25-1 through 25-3 (that is, when employees accept the offer).

**Example 4: Costs to Terminate an Operating Lease**

55-11 This Example illustrates the guidance in paragraphs 420-10-25-11 through 25-13 and paragraphs 420-10-30-7 through 30-9 related to terminating an operating lease at the cease-use date and after the cease-use date.

**Pending Content (Transition Guidance: ASC 842-10-65-1)**

55-11 Paragraph superseded by Accounting Standards Update No. 2016-02.

55-12 An entity leases a facility under an operating lease that requires the entity to pay lease rentals of $100,000 per year for 10 years. After using the facility for five years, the entity commits to an exit plan. In connection with that plan, the entity will cease using the facility in 1 year (after using the facility for 6 years), at which time the remaining lease rentals will be $400,000 ($100,000 per year for the remaining term of 4 years). In accordance with paragraphs 420-10-30-7 through 30-9, a liability for the remaining lease rentals, reduced by actual (or estimated) sublease rentals, would be recognized and measured at its fair value at the cease-use date (as illustrated in the following paragraph). In accordance with paragraphs 420-10-35-1 through 35-4, the liability would be adjusted for changes, if any, resulting from revisions to estimated cash flows after the cease-use date, measured using the credit-adjusted risk-free rate that was used to measure the liability initially (as illustrated in paragraph 420-10-55-15).

**Pending Content (Transition Guidance: ASC 842-10-65-1)**

55-12 Paragraph superseded by Accounting Standards Update No. 2016-02.

55-13 Based on market rentals for similar leased property, the entity determines that if it desired, it could sublease the facility and receive sublease rentals of $300,000 ($75,000 per year for the remaining lease term of 4 years). However, for competitive reasons, the entity decides not to sublease the facility (or otherwise terminate the lease) at the cease-use date. The fair value of the liability at the cease-use date is $89,427, estimated using an expected present value technique. The expected net cash flows of $100,000 ($25,000 per year for the remaining lease term of 4 years) are discounted using a credit-adjusted risk-free rate of 8 percent. In this case, a risk premium is not considered in the present value measurement. Because the lease rentals are fixed by contract and the estimated sublease rentals are based on market prices for similar leased property for other entities having similar credit standing as the entity, there is little uncertainty in the amount and timing of the expected cash flows used in estimating fair value at the cease-use date and any risk premium would be insignificant. In other circumstances, a risk premium would be appropriate if it is significant. Thus, a liability (expense) of $89,427 would be recognized at the cease-use date.
10.10.8.2 Operating-Lease Termination Costs

ASC 842 addresses the accounting for the costs of terminating a lease contract. However, before the adoption of ASC 842, such costs were addressed in ASC 420-10-25-11. The discussion in this subsection applies only to entities that have not yet adopted ASC 842.

Before the adoption of ASC 842, ASC 420-10-25-11 stated, in part:

For purposes of this Subtopic, costs to terminate an operating lease or other contract are either of the following:

a. Costs to terminate the contract before the end of its term
b. Costs that will continue to be incurred under the contract for its remaining term without economic benefit to the entity.

Further, ASC 420-10-30-7 and 30-8 stated:

A liability for costs to terminate a contract before the end of its term shall be measured at its fair value when the entity terminates the contract in accordance with the contract terms (for example, when the entity gives written notice to the counterparty within the notification period specified by the contract or has otherwise negotiated a termination with the counterparty).

If the contract is an operating lease, the fair value of the liability at the cease-use date shall be determined based on the remaining lease rentals, adjusted for the effects of any prepaid or deferred items recognized under the lease, and reduced by estimated sublease rentals that could be reasonably obtained for the property, even if the entity does not intend to enter into a sublease. Remaining lease rentals shall not be reduced to an amount less than zero.
In accordance with the above guidance, when an entity ceases using the rights conveyed under an operating lease, the contract termination costs must be recognized as a liability at fair value. Contract termination costs include either (1) the costs of terminating the contract before the end of its term or (2) the costs that will continue to be incurred under a contract for its remaining term without economic benefit to the entity. ASC 420-10-30-8 indicates that “[i]f the contract is an operating lease, the fair value of the liability” as of the date on which the entity ceases using the benefits conveyed by the lease should be measured on the basis of the remaining lease rentals, “reduced by estimated sublease rentals that could be reasonably obtained for the property” (emphasis added). Therefore, even if an entity has no intention of subleasing the property, perhaps for competitive reasons, the entity is required to estimate sublease rentals that could be obtained for the property and to reduce future contractual rentals by this estimated sublease income in measuring the fair value of the liability associated with the abandoned operating lease. In making these estimates, the entity will most likely have to consult with leasing brokers, real estate agents, or other experts with knowledge of current market rents for the property in question.

In determining the fair value of a liability associated with a property subject to an operating lease that will cease being used, it may be appropriate to assume sublease income of zero for a short period after the cease-use date. This assumption, which is consistent with the fair value measurement requirements of ASC 420-10 (in accordance with ASC 820), is based on the fact that even if an entity decided to sublease an abandoned property, administratively it would take a short time to execute the necessary agreements to get the sublease tenant in place. The sublease closing period would include the average time it would take to negotiate, draft, and execute a sublease for the property and would vary depending on the entity's specific facts and circumstances.

Initial direct costs (e.g., commissions and legal fees) that would be incurred in connection with obtaining a sublease should be included in the calculation of the fair value of the liability recognized for contract termination costs associated with an operating lease. Such costs are included in the fair value estimate by reducing the estimated cash inflows from sublease rentals. This guidance is analogous to that in ASC 420-10-30-8 related to the primary lease. Specifically, ASC 420-10-30-8 indicates that “the remaining lease rentals [should be] adjusted for the effects of any prepaid or deferred items recognized under the lease.” Therefore, the present value of the initial direct costs will increase the liability and related expense as of the cease-use date.

10.10.9 Guarantees

<table>
<thead>
<tr>
<th>ASC 460-10</th>
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<tbody>
<tr>
<td><strong>Fair Value Objective</strong></td>
</tr>
<tr>
<td>30-2 Except as indicated in paragraphs 460-10-30-3 through 30-4, the objective of the initial measurement of a guarantee liability is the fair value of the guarantee at its inception. For example:</td>
</tr>
<tr>
<td>a. If a guarantee is issued in a standalone arm's-length transaction with an unrelated party, the liability recognized at the inception of the guarantee shall be the premium received or receivable by the guarantor as a practical expedient.</td>
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<tr>
<td>b. If a guarantee is issued as part of a transaction with multiple elements with an unrelated party (such as in conjunction with selling an asset or entering into an operating lease), the liability recognized at the inception of the guarantee should be an estimate of the guarantee's fair value. In that circumstance, a guarantor shall consider what premium would be required by the guarantor to issue the same guarantee in a standalone arm's-length transaction with an unrelated party as a practical expedient.</td>
</tr>
<tr>
<td>c. If a guarantee is issued as a contribution to an unrelated party, the liability recognized at the inception of the guarantee shall be measured at its fair value, consistent with the requirement to measure the contribution made at fair value, as prescribed in Section 720-25-30. For related implementation guidance, see paragraph 460-10-55-14.</td>
</tr>
</tbody>
</table>
**Chapter 10 — Subsequent Measurement**

**ASC 460-10 (continued)**

**Pending Content (Transition Guidance: ASC 842-10-65-1)**

**30-2** Except as indicated in paragraphs 460-10-30-3 through 30-4, the objective of the initial measurement of a guarantee liability is the fair value of the guarantee at its inception. For example:

a. If a guarantee is issued in a standalone arm's-length transaction with an unrelated party, the liability recognized at the inception of the guarantee shall be the premium received or receivable by the guarantor as a practical expedient.

b. If a guarantee is issued as part of a transaction with multiple elements with an unrelated party (such as in conjunction with selling an asset), the liability recognized at the inception of the guarantee should be an estimate of the guarantee's fair value. In that circumstance, a guarantor shall consider what premium would be required by the guarantor to issue the same guarantee in a standalone arm's-length transaction with an unrelated party as a practical expedient.

c. If a guarantee is issued as a contribution to an unrelated party, the liability recognized at the inception of the guarantee shall be measured at its fair value, consistent with the requirement to measure the contribution made at fair value, as prescribed in Section 720-25-30. For related implementation guidance, see paragraph 460-10-55-14.

**Pending Content (Transition Guidance: ASC 326-10-65-1)**

**30-2** Except as indicated in paragraphs 460-10-30-3 through 30-5, the objective of the initial measurement of a guarantee liability is the fair value of the guarantee at its inception. For example:

a. If a guarantee is issued in a standalone arm's-length transaction with an unrelated party, the liability recognized at the inception of the guarantee shall be the premium received or receivable by the guarantor as a practical expedient.

b. If a guarantee is issued as part of a transaction with multiple elements with an unrelated party (such as in conjunction with selling an asset), the liability recognized at the inception of the guarantee should be an estimate of the guarantee's fair value. In that circumstance, a guarantor shall consider what premium would be required by the guarantor to issue the same guarantee in a standalone arm's-length transaction with an unrelated party as a practical expedient.

c. If a guarantee is issued as a contribution to an unrelated party, the liability recognized at the inception of the guarantee shall be measured at its fair value, consistent with the requirement to measure the contribution made at fair value, as prescribed in Section 720-25-30. For related implementation guidance, see paragraph 460-10-55-14.

**Probable Contingent Losses for Which the Amount of Loss Can Be Reasonably Estimated**

**30-4** For many guarantors, it would be unusual at the inception of the guarantee for the contingent liability amount under (b) in the preceding paragraph to exceed the amount that satisfies the fair value objective under (a) in the preceding paragraph. An example of that unusual circumstance is a guarantee for which, at inception, there is a high (probable) likelihood that the guarantor will be required to pay the maximum potential settlement at the end of the six-month term and a low likelihood that the guarantor will not be required to make any payment at the end of the six-month term. The amount that satisfies the fair value objective would include consideration of the low likelihood that no payment will be required, but the accrual of the contingent loss under Section 450-20-30 would be based solely on the best estimate of the settlement amount whose payment is probable (the maximum potential settlement amount in this case). This example is considered to be an unusual circumstance because of the high likelihood at inception that the maximum potential settlement amount will be paid, resulting in a substantial initial fair value for that guarantee. Another example in which the contingent liability amount required to be recognized under (b) in the preceding paragraph exceeds the fair value at inception under (a) in the preceding paragraph would involve an undiscounted accrual under Subtopic 450-20 for a guarantee payment that is expected to occur many years in the future.
In many cases, the one-time premium received by a guarantor for issuing a guarantee will be an appropriate practical expedient for the initial measurement of the guarantee obligation (see paragraph 460-10-30-2[a]). However, if a one-time premium is specified for a guarantee that is issued in conjunction with another transaction (such as the sale of assets by the guarantor), the specified premium may not be an appropriate initial measurement of the guarantor's liability because the amount specified as being applicable to the guarantee may or may not be its fair value (see paragraph 460-10-30-2[b]).

**10.10.10 Other Liabilities**

**10.10.10.1 Convertible Debt**

**ASC 470-20**

**Instrument Issued as Repayment for Nonconvertible Instrument**

30-19 If a convertible instrument is issued as repayment of a nonconvertible instrument at the nonconvertible instrument's maturity, the fair value of the newly issued convertible instrument shall be the redemption amount owed at the maturity date of the original instrument if both of the following conditions exist:

a. The original instrument has matured.

b. The exchange of debt instruments is not a troubled debt restructuring that would be accounted for by the issuer under Subtopic 470-60.

**Convertible Instruments Issued to Nonemployees for Goods and Services**

30-25 All of the following guidelines for determining the fair value of convertible instruments shall be used:

a. If the fair value of the goods or services received is reliably determinable, and the issuer has not recently issued similar convertible instruments, the fair value of the goods or services shall be used to measure the transaction.

b. Recent issuances of similar convertible instruments for cash to parties that only have an investor relationship with the issuer may provide the best evidence of fair value of the convertible instrument.

c. If reliable information under (a) or (b) is not available, the fair value of the convertible instrument shall be deemed to be no less than the fair value of the equity shares into which it can be converted.

**Pending Content (Transition Guidance: ASC 718-10-65-11)**

30-25 Both of the following guidelines for determining the fair value of convertible instruments shall be used:

b. Recent issuances of similar convertible instruments for cash to parties that only have an investor relationship with the issuer may provide the best evidence of fair value of the convertible instrument.

c. If reliable information under (b) is not available, the fair value of the convertible instrument shall be deemed to be no less than the fair value of the equity shares into which it can be converted.

**Liability Component**

35-14 If, under Subtopic 820-10, an issuer uses a valuation technique consistent with an income approach to measure the fair value of the liability component at initial recognition, the issuer shall consider the periods of cash flows used in the fair value measurement when determining the appropriate discount amortization period.
For additional discussion of the borrowing rate used to determine the fair value of the liability component of a convertible debt instrument within the scope of the cash conversion subsections of ASC 470-20, see Section 6.3.2 of Deloitte’s *A Roadmap to the Issuer’s Accounting for Convertible Debt*.

### 10.10.10.2 Physically Settled Forward Purchase Contracts

**ASC 480-10**

**Certain Physically Settled Forward Purchase Contracts**

30-3 Forward contracts that require physical settlement by repurchase of a fixed number of the issuer’s equity shares in exchange for cash shall be measured initially at the fair value of the shares at inception, adjusted for any consideration or unstated rights or privileges.

30-4 Two ways to obtain the adjusted fair value include:

a. Determining the amount of cash that would be paid under the conditions specified in the contract if the shares were repurchased immediately

b. Discounting the settlement amount, at the rate implicit at inception after taking into account any consideration or unstated rights or privileges that may have affected the terms of the transaction.

### 10.10.11 Assets of a Defined Benefit Pension or Other Postretirement Plan

**ASC 715-30**

**Annuity and Other Contracts**

35-60 Insurance contracts that are in substance equivalent to the purchase of annuities shall be accounted for as such. Other contracts with insurance entities shall be accounted for as investments and measured at fair value. For some contracts, the best available evidence of fair value may be contract value. If a contract has a determinable cash surrender value or conversion value, that is presumed to be its fair value.

**Selection of Discount Rates**

55-30 Use of assumed discount rates based on historical rates of return is inconsistent with the paragraph 715-30-35-50 requirement to value plan assets at fair value. If interest rates decline or rise, the effect of the requirement to use current rates is to increase or decrease the present value of the projected benefit obligation. That increase or decrease in the obligation is a loss or gain that would be offset to the extent of the gain or loss in the fair value of the plan’s dedicated portfolio of fixed-income investments. Any net gain or loss is subject to amortization as a component of net periodic pension cost.

**Insurance Contracts**

55-42 Guaranteed investment contracts are not annuity contracts because they transfer only investment risk to the insurer. The insurer does not unconditionally undertake a legal obligation to provide specified pension benefits to specific individuals. For a guaranteed investment contract with a specified maturity date and for which there is no intent to liquidate the contract before that date, evidence of the fair value of the guaranteed investment contract might be obtained by looking to current yields on fixed-maturity securities having similar risk characteristics and duration.

55-43 In an immediate participation guarantee investment contract, the market value adjustment should be considered in determining its fair value because, in effect, the contract value adjusted for any such market value adjustment represents the cash surrender value referred to in paragraph 715-30-35-60. If an immediate participation guarantee investment contract can be converted into an annuity contract, the conversion value of the contract should be considered in determining its fair value. The evidence of fair value noted for guaranteed investment contracts in the preceding paragraph should also be considered for immediate participation guarantee investment contracts.
35-120 Other contracts with insurance entities may not meet the definition of an insurance contract because the insurance entity does not unconditionally undertake a legal obligation to provide specified benefits to specified individuals. Those contracts shall be accounted for as investments and measured at fair value. If a contract has a determinable cash surrender value or conversion value, that is presumed to be its fair value. For some contracts, the best available estimate of fair value may be contract value.

10.10.12 Contributions

30-2 Unconditional promises to give that are expected to be paid in less than one year may be measured at net settlement value because that amount, although not equivalent to the present value of estimated future cash flows, results in a reasonable estimate of fair value.

10.10.13 Business Combinations

30-3 The following guidance demonstrates the application of the measurement principle in paragraph 805-20-30-1 to specific situations in a business combination including guidance on measuring the fair values of particular identifiable assets and a noncontrolling interest in an acquiree.

Assets With Uncertain Cash Flows (Valuation Allowances)

30-4 The acquirer shall not recognize a separate valuation allowance as of the acquisition date for assets acquired in a business combination that are measured at their acquisition-date fair values because the effects of uncertainty about future cash flows are included in the fair value measure. For example, because this Subtopic requires the acquirer to measure acquired receivables, including loans, at their acquisition-date fair values, the acquirer does not recognize a separate valuation allowance for the contractual cash flows that are deemed to be uncollectible at that date.

Pending Content (Transition Guidance: ASC 326-10-65-1)

30-4 The acquirer shall not recognize a separate valuation allowance as of the acquisition date for assets acquired in a business combination that are measured at their acquisition-date fair values because the effects of uncertainty about future cash flows are included in the fair value measure, unless the assets acquired are financial assets for which the acquirer shall refer to the guidance in paragraphs 805-20-30-4A through 30-4B.

30-4A For acquired financial assets that are not purchased financial assets with credit deterioration, the acquirer shall record the purchased financial assets at the acquisition-date fair value. Additionally, for these financial assets within the scope of Topic 326, an allowance shall be recorded with a corresponding charge to credit loss expense as of the reporting date.

30-4B For assets accounted for as purchased financial assets with credit deterioration (which includes beneficial interests that meet the criteria in paragraph 325-40-30-1A), an acquirer shall recognize an allowance in accordance with Topic 326 with a corresponding increase to the amortized cost basis of the financial asset(s) as of the acquisition date.
ASC 805-20 (continued)

**Assets Subject to Operating Leases in Which the Acquiree Is the Lessor**

30-5 The acquirer shall measure the acquisition-date fair value of an asset, such as a building or a patent or other intangible asset, that is subject to an operating lease in which the acquiree is the lessor separately from the lease contract. In other words, the fair value of the asset shall be the same regardless of whether it is subject to an operating lease. In accordance with paragraph 805-20-25-12, the acquirer separately recognizes an asset or a liability if the terms of the lease are favorable or unfavorable relative to market terms.

**Assets That the Acquirer Intends Not to Use or to Use in a Way Other Than Their Highest and Best Use**

30-6 To protect its competitive position, or for other reasons, the acquirer may intend not to use an acquired nonfinancial asset actively, or it may not intend to use the asset according to its highest and best use. For example, that might be the case for an acquired research and development intangible asset that the acquirer plans to use defensively by preventing others from using it. Nevertheless, the acquirer shall measure the fair value of the nonfinancial asset in accordance with Subtopic 820-10 assuming its highest and best use by market participants in accordance with the appropriate valuation premise, both initially and for purposes of subsequent impairment testing.

**Measuring the Fair Value of a Noncontrolling Interest in an Acquiree**

30-7 Paragraph 805-20-30-1 requires the acquirer to measure a noncontrolling interest in the acquiree at its fair value at the acquisition date. An acquirer sometimes will be able to measure the acquisition-date fair value of a noncontrolling interest on the basis of a quoted price in an active market for the equity shares (that is, those not held by the acquirer). In other situations, however, a quoted price in an active market for the equity shares will not be available. In those situations, the acquirer would measure the fair value of the noncontrolling interest using another valuation technique.

30-8 The fair values of the acquirer's interest in the acquiree and the noncontrolling interest on a per-share basis might differ. The main difference is likely to be the inclusion of a control premium in the per-share fair value of the acquirer's interest in the acquiree or, conversely, the inclusion of a discount for lack of control (also referred to as a noncontrolling interest discount) in the per-share fair value of the noncontrolling interest if market participants would take into account such a premium or discount when pricing the noncontrolling interest.

**Measurement of Assets and Liabilities Arising From Contingencies**

30-9 Paragraphs 805-20-25-18A through 25-20B establish the requirements related to recognition of certain assets and liabilities arising from contingencies. Initial measurement of assets and liabilities meeting the recognition criteria in paragraph 805-20-25-19 shall be at acquisition-date fair value. Guidance on the initial measurement of other assets and liabilities from contingencies not meeting the recognition criteria of that paragraph, but meeting the criteria in paragraph 805-20-25-20 is at paragraph 805-20-30-23.

**Indemnification Assets**

30-18 Paragraph 805-20-25-27 requires that the acquirer recognize an indemnification asset at the same time that it recognizes the indemnified item, measured on the same basis as the indemnified item, subject to the need for a valuation allowance for uncollectible amounts. That paragraph also requires that, if the indemnification relates to an asset or a liability that is recognized at the acquisition date and measured at its acquisition-date fair value, the acquirer recognize the indemnification asset at the acquisition date measured at its acquisition-date fair value. For an indemnification asset measured at fair value, the effects of uncertainty about future cash flows because of collectibility considerations are included in the fair value measure and a separate valuation allowance is not necessary, as noted in paragraph 805-20-30-4.

**Reacquired Rights**

30-20 The acquirer shall measure the value of a reacquired right recognized as an intangible asset in accordance with paragraph 805-20-25-14 on the basis of the remaining contractual term of the related contract regardless of whether market participants would consider potential contractual renewals in determining its fair value.
ASC 805-20 (continued)

Recognition of Intangible Assets Separately From Goodwill

55-2 Paragraph 805-20-25-10 establishes that an intangible asset is identifiable if it meets either the separability criterion or the contractual-legal criterion described in the definition of identifiable. An intangible asset that meets the contractual-legal criterion is identifiable even if the asset is not transferable or separable from the acquiree or from other rights and obligations. For example:

a. An acquiree leases a manufacturing facility under an operating lease that has terms that are favorable relative to market terms. The lease terms explicitly prohibit transfer of the lease (through either sale or sublease). The amount by which the lease terms are favorable compared with the pricing of current market transactions for the same or similar items is an intangible asset that meets the contractual-legal criterion for recognition separately from goodwill, even though the acquirer cannot sell or otherwise transfer the lease contract. See also paragraphs 805-20-25-12 through 25-13.

b. An acquiree owns and operates a nuclear power plant. The license to operate that power plant is an intangible asset that meets the contractual-legal criterion for recognition separately from goodwill, even if the acquirer cannot sell or transfer it separately from the acquired power plant. An acquirer may recognize the fair value of the operating license and the fair value of the power plant as a single asset for financial reporting purposes if the useful lives of those assets are similar.

c. An acquiree owns a technology patent. It has licensed that patent to others for their exclusive use outside the domestic market, receiving a specified percentage of future foreign revenue in exchange. Both the technology patent and the related license agreement meet the contractual-legal criterion for recognition separately from goodwill even if selling or exchanging the patent and the related license agreement separately from one another would not be practical.

Pending Content (Transition Guidance: ASC 842-10-65-1)

55-2 Paragraph 805-20-25-10 establishes that an intangible asset is identifiable if it meets either the separability criterion or the contractual-legal criterion described in the definition of identifiable. An intangible asset that meets the contractual-legal criterion is identifiable even if the asset is not transferable or separable from the acquiree or from other rights and obligations. For example:

a. An acquiree leases a manufacturing facility to a lessee under an operating lease that has terms that are favorable relative to market terms. The lease terms explicitly prohibit transfer of the lease (through either sale or sublease). The amount by which the lease terms are favorable compared with the pricing of current market transactions for the same or similar items is an intangible asset that meets the contractual-legal criterion for recognition separately from goodwill, even though the acquirer cannot sell or otherwise transfer the lease contract. See also paragraph 805-20-25-12.

b. An acquiree owns and operates a nuclear power plant. The license to operate that power plant is an intangible asset that meets the contractual-legal criterion for recognition separately from goodwill, even if the acquirer cannot sell or transfer it separately from the acquired power plant. An acquirer may recognize the fair value of the operating license and the fair value of the power plant as a single asset for financial reporting purposes if the useful lives of those assets are similar.

c. An acquiree owns a technology patent. It has licensed that patent to others for their exclusive use outside the domestic market, receiving a specified percentage of future foreign revenue in exchange. Both the technology patent and the related license agreement meet the contractual-legal criterion for recognition separately from goodwill even if selling or exchanging the patent and the related license agreement separately from one another would not be practical.

Assembled Workforce and Other Items That Are Not Identifiable

55-9 The identifiability criteria determine whether an intangible asset is recognized separately from goodwill. However, the criteria neither provide guidance for measuring the fair value of an intangible asset nor restrict the assumptions used in measuring the fair value of an intangible asset. For example, the acquirer would take into account the assumptions that market participants would use when pricing the intangible asset, such as expectations of future contract renewals, in measuring fair value. It is not necessary for the renewals themselves to meet the identifiability criteria. (However, see paragraph 805-20-30-20, which establishes an exception to the fair value measurement principle for reacquired rights recognized in a business combination.)
ASC 805-20 (continued)

Servicing Contracts Such as Mortgage Servicing Contracts

55-35 If mortgage loans, credit card receivables, or other financial assets are acquired in a business combination with the servicing obligation, the inherent servicing rights are not a separate intangible asset because the fair value of those servicing rights is included in the measurement of the fair value of the acquired financial asset.

Case B: One Customer, Contract in One of Two Lines of Business

55-55 Target manufactures goods in two distinct lines of business: sporting goods and electronics. Customer purchases both sporting goods and electronics from Target. Target has a contract with Customer to be its exclusive provider of sporting goods but has no contract for the supply of electronics to Customer. Both Target and Acquirer believe that only one overall customer relationship exists between Target and Customer. The contract to be Customer’s exclusive supplier of sporting goods, whether cancelable or not, meets the contractual-legal criterion. Additionally, because Target establishes its relationship with Customer through a contract, the customer relationship with Customer meets the contractual-legal criterion. Because Target has only one customer relationship with Customer, the fair value of that relationship incorporates assumptions about Target’s relationship with Customer related to both sporting goods and electronics. However, if Acquirer determines that the customer relationships with Customer for sporting goods and for electronics are separate from each other, Acquirer would assess whether the customer relationship for electronics meets the separability criterion for identification as an intangible asset.

ASC 805-30

Measurement of Goodwill

30-2 In a business combination in which the acquirer and the acquiree (or its former owners) exchange only equity interests, the acquisition-date fair value of the acquiree’s equity interests may be more reliably measurable than the acquisition-date fair value of the acquirer’s equity interests. If so, the acquirer shall determine the amount of goodwill by using the acquisition-date fair value of the acquiree’s equity interests instead of the acquisition-date fair value of the equity interests transferred.

30-3 To determine the amount of goodwill in a business combination in which no consideration is transferred, the acquirer shall use the acquisition-date fair value of the acquirer’s interest in the acquiree determined using a valuation technique in place of the acquisition-date fair value of the consideration transferred (see paragraph 805-30-30-1(a)(1)). Paragraphs 805-30-55-3 through 55-5 provide additional guidance on applying the acquisition method to combinations of mutual entities, including measuring the acquisition-date fair value of the acquiree’s equity interests using a valuation technique.

Consideration Transferred

30-7 The consideration transferred in a business combination shall be measured at fair value, which shall be calculated as the sum of the acquisition-date fair values of the assets transferred by the acquirer, the liabilities incurred by the acquirer to former owners of the acquiree, and the equity interests issued by the acquirer. (However, any portion of the acquiree’s share-based payment awards exchanged for awards held by the acquiree’s employees that is included in consideration transferred in the business combination shall be measured in accordance with paragraph 805-20-30-21 rather than at fair value.) Examples of potential forms of consideration include the following:

a. Cash
b. Other assets
c. A business or a subsidiary of the acquirer
d. Contingent consideration (see paragraphs 805-30-25-5 through 25-7)
e. Common or preferred equity instruments
f. Options
g. Warrants
h. Member interests of mutual entities.
### Pending Content (Transition Guidance: ASC 718-10-65-11)

**30-7** The consideration transferred in a business combination shall be measured at fair value, which shall be calculated as the sum of the acquisition-date fair values of the assets transferred by the acquirer, the liabilities incurred by the acquirer to former owners of the acquiree, and the equity interests issued by the acquirer. (However, any portion of the acquirer's share-based payment awards exchanged for awards held by the acquiree's grantees that is included in consideration transferred in the business combination shall be measured in accordance with paragraph 805-20-30-21 rather than at fair value.) Examples of potential forms of consideration include the following:

- a. Cash
- b. Other assets
- c. A business or a subsidiary of the acquirer
- d. Contingent consideration (see paragraphs 805-30-25-5 through 25-7)
- e. Common or preferred equity instruments
- f. Options
- g. Warrants
- h. Member interests of mutual entities.

**30-8** The consideration transferred may include assets or liabilities of the acquirer that have carrying amounts that differ from their fair values at the acquisition date (for example, nonmonetary assets or a business of the acquirer). If so, the acquirer shall remeasure the transferred assets or liabilities to their fair values as of the acquisition date and recognize the resulting gains or losses, if any, in earnings. However, sometimes the transferred assets or liabilities remain within the combined entity after the business combination (for example, because the assets or liabilities were transferred to the acquiree rather than to its former owners), and the acquirer therefore retains control of them. In that situation, the acquirer shall measure those assets and liabilities at their carrying amounts immediately before the acquisition date and shall not recognize a gain or loss in earnings on assets or liabilities it controls both before and after the business combination.

### Measuring the Acquisition-Date Fair Value of the Acquirer’s Interest in the Acquiree Using Valuation Techniques

**55-2** In a business combination achieved without the transfer of consideration, the acquirer must substitute the acquisition-date fair value of its interest in the acquiree for the acquisition-date fair value of the consideration transferred to measure goodwill or a gain on a bargain purchase (see paragraphs 805-30-30-1 through 30-4). Subtopic 820-10 provides guidance on using valuation techniques to measure fair value.

### Special Consideration in Applying the Acquisition Method to Combinations of Mutual Entities

**55-3** When two mutual entities combine, the fair value of the equity or member interests in the acquiree (or the fair value of the acquiree) may be more reliably measurable than the fair value of the member interests transferred by the acquirer. In that situation, paragraph 805-30-30-2 through 30-3 requires the acquirer to determine the amount of goodwill by using the acquisition-date fair value of the acquiree's equity interests instead of the acquisition-date fair value of the acquiree's equity interests transferred as consideration. In addition, the acquirer in a combination of mutual entities shall recognize the acquiree's net assets as a direct addition to capital or equity in its statement of financial position, not as an addition to retained earnings, which is consistent with the way in which other types of entities apply the acquisition method.

**55-4** Although they are similar in many ways to other businesses, mutual entities have distinct characteristics that arise primarily because their members are both customers and owners. Members of mutual entities generally expect to receive benefits for their membership, often in the form of reduced fees charged for goods and services or patronage dividends. The portion of patronage dividends allocated to each member is often based on the amount of business the member did with the mutual entity during the year.
A fair value measurement of a mutual entity should include the assumptions that market participants would make about future member benefits as well as any other relevant assumptions market participants would make about the mutual entity. For example, an estimated cash flow model may be used to determine the fair value of a mutual entity. The cash flows used as inputs to the model should be based on the expected cash flows of the mutual entity, which are likely to reflect reductions for member benefits, such as reduced fees charged for goods and services.

Measuring the Consideration Transferred

In a reverse acquisition, the accounting acquirer usually issues no consideration for the acquiree. Instead, the accounting acquiree usually issues its equity shares to the owners of the accounting acquirer. Accordingly, the acquisition-date fair value of the consideration transferred by the accounting acquirer for its interest in the accounting acquiree is based on the number of equity interests the legal subsidiary would have had to issue to give the owners of the legal parent the same percentage equity interest in the combined entity that results from the reverse acquisition. Example 1, Case A (see paragraph 805-40-55-8) illustrates that calculation. The fair value of the number of equity interests calculated in that way can be used as the fair value of consideration transferred in exchange for the acquiree.

Case A: All the Shares of the Legal Subsidiary Are Exchanged

This Case illustrates the accounting for a reverse acquisition if all of the shares of the legal subsidiary, the accounting acquirer, are exchanged in a business combination. The accounting illustrated in this Case includes the calculation of the fair value of the consideration transferred, the measurement of goodwill and the calculation of earnings per share (EPS).

The calculation of the fair value of the consideration transferred follows.

As a result of the issuance of 150 common shares by Entity A (legal parent, accounting acquiree), Entity B's shareholders own 60 percent of the issued shares of the combined entity, that is, 150 of 250 issued shares. The remaining 40 percent are owned by Entity A's shareholders. If the business combination had taken the form of Entity B issuing additional common shares to Entity A's shareholders in exchange for their common shares in Entity A, Entity B would have had to issue 40 shares for the ratio of ownership interest in the combined entity to be the same. Entity B's shareholders would then own 60 of the 100 issued shares of Entity B — 60 percent of the combined entity. As a result, the fair value of the consideration effectively transferred by Entity B and the group's interest in Entity A is $1,600 (40 shares with a per-share fair value of $40). The fair value of the consideration effectively transferred should be based on the most reliable measure. In this Case, the quoted market price of Entity A's shares provides a more reliable basis for measuring the consideration effectively transferred than the estimated fair value of the shares in Entity B, and the consideration is measured using the market price of Entity A's shares — 100 shares with a per-share fair value of $16.

Goodwill is measured as follows.
Goodwill is measured as the excess of the fair value of the consideration effectively transferred (the group's interest in Entity A) over the net amount of Entity A's recognized identifiable assets and liabilities, as follows.

<table>
<thead>
<tr>
<th></th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consideration effectively transferred</td>
<td>1,600</td>
</tr>
<tr>
<td>Net recognized values of Entity A's identifiable assets and liabilities</td>
<td></td>
</tr>
<tr>
<td>Current assets</td>
<td>500</td>
</tr>
<tr>
<td>Noncurrent assets</td>
<td>1,500</td>
</tr>
<tr>
<td>Current liabilities</td>
<td>(300)</td>
</tr>
<tr>
<td>Noncurrent liabilities</td>
<td>(400)</td>
</tr>
<tr>
<td>Goodwill</td>
<td>300</td>
</tr>
</tbody>
</table>

The consolidated statement of financial position immediately after the business combination is as follows.

<table>
<thead>
<tr>
<th></th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current assets ($700 + $500)</td>
<td>1,200</td>
</tr>
<tr>
<td>Noncurrent assets ($3,000 + $1,500)</td>
<td>4,500</td>
</tr>
<tr>
<td>Goodwill</td>
<td>300</td>
</tr>
<tr>
<td>Total assets</td>
<td>6,000</td>
</tr>
<tr>
<td>Current liabilities ($600 + $300)</td>
<td>900</td>
</tr>
<tr>
<td>Noncurrent liabilities ($1,100 + $400)</td>
<td>1,500</td>
</tr>
<tr>
<td>Total liabilities</td>
<td>2,400</td>
</tr>
</tbody>
</table>

Shareholders' equity

<table>
<thead>
<tr>
<th></th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retained earnings</td>
<td>1,400</td>
</tr>
<tr>
<td>Issued equity</td>
<td></td>
</tr>
<tr>
<td>250 common shares ($600 + $1,600)</td>
<td>2,200</td>
</tr>
<tr>
<td>Total shareholders' equity</td>
<td>3,600</td>
</tr>
<tr>
<td>Total liabilities and shareholders' equity</td>
<td>6,000</td>
</tr>
</tbody>
</table>

In accordance with paragraph 805-40-45-2(c) through (d), the amount recognized as issued equity interests in the consolidated financial statements ($2,200) is determined by adding the issued equity of the legal subsidiary immediately before the business combination ($600) and the fair value of the consideration effectively transferred, measured in accordance with paragraph 805-40-30-2 ($1,600). However, the equity structure appearing in the consolidated financial statements (that is, the number and type of equity interests issued) must reflect the equity structure of the legal parent, including the equity interests issued by the legal parent to effect the combination.
Chapter 10 — Subsequent Measurement

ASC 805-40 (continued)

55-15 The calculation of EPS follows.

55-16 Entity B’s earnings for the annual period ended December 31, 20X5, were $600, and the consolidated earnings for the annual period ended December 31, 20X6, are $800. There was no change in the number of common shares issued by Entity B during the annual period ended December 31, 20X5, and during the period from January 1, 20X6, to the date of the reverse acquisition on September 30, 20X6. EPS for the annual period ended December 31, 20X6, is calculated as follows.

Number of shares deemed to be outstanding for the period from January 1, 20X6, to the acquisition date (that is, the number of common shares issued by Entity A [legal parent, accounting acquiree] in the reverse acquisition) 150

Number of shares outstanding from the acquisition date to December 31, 20X6 250

Weighted-average number of common shares outstanding \((150 \times 9 + 250 \times 3) / 12\) 175

EPS \(800 \div 175\) $4.57

55-17 Restated EPS for the annual period ending December 31, 20X5, is $4.00 (calculated as the earnings of Entity B of 600 divided by the 150 common shares Entity A issued in the reverse acquisition).

Case B: Not All the Shares of the Legal Subsidiary Are Exchanged

55-18 This Case illustrates the accounting for a reverse acquisition if not all of the shares of the legal subsidiary, the accounting acquirer, are exchanged in a business combination and a noncontrolling interest results.

55-19 Assume the same facts as in Case A except that only 56 of Entity B’s 60 common shares are exchanged. Because Entity A issues 2.5 shares in exchange for each common share of Entity B, Entity A issues only 140 (rather than 150) shares. As a result, Entity B’s shareholders own 58.3 percent of the issued shares of the combined entity (140 of 240 issued shares). The fair value of the consideration transferred for Entity A, the accounting acquiree, is calculated by assuming that the combination had been effected by Entity B’s issuing additional common shares to the shareholders of Entity A in exchange for their common shares in Entity A. That is because Entity B is the accounting acquirer, and paragraphs 805-30-30-7 through 30-8 require the acquirer to measure the consideration exchanged for the accounting acquiree.

55-20 In calculating the number of shares that Entity B would have had to issue, the noncontrolling interest is ignored. The majority shareholders own 56 shares of Entity B. For that to represent a 58.3 percent equity interest, Entity B would have had to issue an additional 40 shares. The majority shareholders would then own 56 of the 96 issued shares of Entity B and, therefore, 58.3 percent of the combined entity. As a result, the fair value of the consideration transferred for Entity A, the accounting acquiree, is $1,600 (that is, 40 shares each with a fair value of $40). That is the same amount as when all 60 of Entity B’s shareholders tender all 60 of its common shares for exchange. The recognized amount of the group’s interest in Entity A, the accounting acquiree, does not change if some of Entity B’s shareholders do not participate in the exchange.

55-21 The noncontrolling interest is represented by the 4 shares of the total 60 shares of Entity B that are not exchanged for shares of Entity A. Therefore, the noncontrolling interest is 6.7 percent. The noncontrolling interest reflects the noncontrolling shareholders’ proportionate interests in the precombination carrying amounts of the net assets of Entity B, the legal subsidiary. Therefore, the consolidated statement of financial position is adjusted to show a noncontrolling interest of 6.7 percent of the precombination carrying amounts of Entity B’s net assets (that is, $134 or 6.7 percent of $2,000).
**The consolidated statement of financial position at September 30, 20X6, reflecting the noncontrolling interest is as follows.**

<table>
<thead>
<tr>
<th></th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current assets ($700 + $500)</td>
<td>1,200</td>
</tr>
<tr>
<td>Noncurrent assets ($3,000 + $1,500)</td>
<td>4,500</td>
</tr>
<tr>
<td>Goodwill</td>
<td>300</td>
</tr>
<tr>
<td><strong>Total assets</strong></td>
<td><strong>6,000</strong></td>
</tr>
<tr>
<td>Current liabilities ($600 + $300)</td>
<td>900</td>
</tr>
<tr>
<td>Noncurrent liabilities ($1,100 + $400)</td>
<td>1,500</td>
</tr>
<tr>
<td><strong>Total liabilities</strong></td>
<td><strong>2,400</strong></td>
</tr>
</tbody>
</table>

**Shareholders’ equity**

<table>
<thead>
<tr>
<th></th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retained earnings ($1,400 × 93.3%)</td>
<td>1,306</td>
</tr>
</tbody>
</table>
| Issued equity
  - 240 common shares ($560 + $1,600) | 2,160 |
| Noncontrolling interest | 134 |
| **Total shareholders’ equity** | **3,600** |
| **Total liabilities and shareholders’ equity** | **6,000** |

The noncontrolling interest of $134 has 2 components. The first component is the reclassification of the noncontrolling interest's share of the accounting acquirer's retained earnings immediately before the acquisition ($1,400 × 6.7% or $93.80). The second component represents the reclassification of the noncontrolling interest's share of the accounting acquirer's issued equity ($600 × 6.7% or $40.20).

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**Determining Cost**

**30-2** Asset acquisitions in which the consideration given is cash are measured by the amount of cash paid, which generally includes the transaction costs of the asset acquisition. However, if the consideration given is not in the form of cash (that is, in the form of noncash assets, liabilities incurred, or equity interests issued) and no other generally accepted accounting principles (GAAP) apply (for example, Topic 845 on nonmonetary transactions or Subtopic 610-20), measurement is based on the cost which shall be measured based on the fair value of the consideration given or the fair value of the assets (or net assets) acquired, whichever is more clearly evident and, thus, more reliably measurable. For transactions involving nonmonetary consideration within the scope of Topic 845, an acquirer must first determine if any of the conditions in paragraph 845-10-30-3 apply. If the consideration given is nonfinancial assets or in substance nonfinancial assets within the scope of Subtopic 610-20, the assets acquired shall be treated as noncash consideration and any gain or loss shall be recognized in accordance with Subtopic 610-20.
In addition to the Codification guidance above, the following guidance may be relevant to the determination of fair value amounts in a business combination:

- Chapters 4 and 5 of Deloitte's *A Roadmap to Accounting for Business Combinations*, which provide additional guidance on fair value measurements in a business combination.
- Section 10.2.7.4.3.1, which discusses the fair value measurement of assumed debt.
- Cases A, B, and C of Example 1 in ASC 820-10-55 (see Sections 5.2.3.4 and 7.4).

### 10.10.14 Derivatives

**ASC 815-10**

35-1A As a practical expedient, a receive-variable, pay-fixed interest rate swap for which the simplified hedge accounting approach (see paragraphs 815-20-25-131AB through 25-131E for scope) is applied may be measured subsequently at settlement value instead of fair value.

35-1B The primary difference between settlement value and fair value is that nonperformance risk is not considered in determining settlement value. One approach for estimating the receive-variable, pay-fixed interest rate swap's settlement value is to perform a present value calculation of the swap's remaining estimated cash flows using a valuation technique that is not adjusted for nonperformance risk.

**ASC 815-15**

**Hybrid Instruments That Are Separated**

30-2 The allocation method that records the embedded derivative at fair value and determines the initial carrying value assigned to the host contract as the difference between the basis of the hybrid instrument and the fair value of the embedded derivative shall be used to determine the carrying values of the host contract component and the embedded derivative component of a hybrid instrument if separate accounting for the embedded derivative is required by this Subtopic. (Note that Section 815-15-25 allows for a fair value election for hybrid financial instruments that otherwise would require bifurcation.)

30-3 The objective is to estimate the fair value of the derivative features separately from the fair value of the nonderivative portions of the contract. Estimates of fair value shall reflect all relevant features of each component. For example, an embedded purchased option that expires if the contract in which it is embedded is prepaid would have a different value than an option whose term is a specified period that is not subject to truncation.

**Limitation on Sum of Component Fair Values**

35-3 If the host contract component of a hybrid instrument is reported at fair value with changes in fair value recognized in earnings or other comprehensive income, then the sum of the fair values of the host contract component and the embedded derivative shall not exceed the overall fair value of the hybrid instrument.
10.10.15 Leases

ASC 840-30

Leveraged Lease Involving an Existing Asset of a Regulated Entity

55-14 As noted in paragraph 840-10-55-46, although the carrying amount of an asset acquired previously may not differ significantly from its fair value, it is unlikely that the two will be the same. However, regulated utilities have argued that the carrying amounts of certain of their assets always equal the fair value based on the utility’s ability to recover that cost in conjunction with a franchise to sell a related service in a specified area. That argument is not valid when considering the value of the asset to a third-party purchaser that does not own that franchise, and it is not consistent with paragraph 840-10-25-43(c).

Pending Content (Transition Guidance: ASC 842-10-65-1)

55-14 Paragraph superseded by Accounting Standards Update No. 2016-02.

ASC 840-40

Criteria for Sale-Leaseback Accounting

25-10 Terms of the sale-leaseback transaction that are substantially different from terms that an independent third-party lessor or lessee would accept represent an exchange of some stated or unstated rights or privileges. Those rights or privileges shall be considered in evaluating the continuing involvement provisions in paragraphs 840-40-25-13 through 25-14 and 840-40-25-17. Those terms or conditions include, but are not limited to, the sales price, the interest rate, and other terms of any loan from the seller-lessee to the buyer-lessee. The fair value of the property used in making that evaluation shall be based on objective evidence, for example, an independent third-party appraisal or recent sales of comparable property.

Pending Content (Transition Guidance: ASC 842-10-65-1)

25-10 Paragraph superseded by Accounting Standards Update No. 2016-02.

ASC 842-30

Fair Value of the Underlying Asset

55-17a Notwithstanding the definition of fair value, if a lessor is not a manufacturer or a dealer, the fair value of the underlying asset at lease commencement is its cost, reflecting any volume or trade discounts that may apply. However, if there has been a significant lapse of time between the acquisition of the underlying asset and lease commencement, the definition of fair value shall be applied.

ASC 842-50

Leveraged Lease Involving an Existing Asset of a Regulated Entity

55-1 Although the carrying amount of an asset acquired previously may not differ significantly from its fair value, it is unlikely that the two will be the same. However, regulated utilities have argued that the carrying amounts of certain of their assets always equal the fair value based on the utility’s ability to recover that cost in conjunction with a franchise to sell a related service in a specified area. That argument is not valid when considering the value of the asset to a third-party purchaser that does not own that franchise.

For more information about how an entity should consider fair value estimates in applying ASC 842, see Deloitte’s A Roadmap to Applying the New Leasing Standard.
10.10.16 Nonmonetary Transactions

**Basic Principle**

30-1 In general, the accounting for nonmonetary transactions should be based on the fair values of the assets (or services) involved, which is the same basis as that used in monetary transactions. Thus, the cost of a nonmonetary asset acquired in exchange for another nonmonetary asset is the fair value of the asset surrendered to obtain it, and a gain or loss shall be recognized on the exchange. The fair value of the asset received shall be used to measure the cost if it is more clearly evident than the fair value of the asset surrendered. Similarly, a nonmonetary asset received in a nonreciprocal transfer shall be recorded at the fair value of the asset received. A transfer of a nonmonetary asset to a stockholder or to another entity in a nonreciprocal transfer shall be recorded at the fair value of the asset transferred and a gain or loss shall be recognized on the disposition of the asset.

30-2 The fair value of an entity's own stock reacquired may be a more clearly evident measure of the fair value of the asset distributed in a nonreciprocal transfer if the transaction involves distribution of a nonmonetary asset to eliminate a disproportionate part of owners' interests (that is, to acquire stock for the treasury or for retirement). If one of the parties in a nonmonetary transaction could have elected to receive cash instead of the nonmonetary asset, the amount of cash that could have been received may be evidence of the fair value of the nonmonetary assets exchanged.

**Commercial Substance**

30-4 A nonmonetary exchange has commercial substance if the entity's future cash flows are expected to significantly change as a result of the exchange. The entity's future cash flows are expected to significantly change if either of the following criteria is met:

a. The configuration (risk, timing, and amount) of the future cash flows of the asset(s) received differs significantly from the configuration of the future cash flows of the asset(s) transferred. The configuration of future cash flows is composed of the risk, timing, and amount of the cash flows. A change in any one of those elements would be a change in configuration.

b. The entity-specific value of the asset(s) received differs from the entity-specific value of the asset(s) transferred, and the difference is significant in relation to the fair values of the assets exchanged. An entity-specific value (referred to as an entity-specific measurement in FASB Concepts Statement No. 7, Using Cash Flow Information and Present Value in Accounting Measurements) is different from a fair value measurement. As described in paragraph 24(b) of Concepts Statement No. 7, an entity-specific value attempts to capture the value of an asset or liability in the context of a particular entity. For example, an entity computing an entity-specific value of an asset would use its expectations about its use of that asset rather than the use assumed by marketplace participants. If it is determined that the transaction has commercial substance, the exchange would be measured at fair value, rather than at the entity-specific value.

A qualitative assessment will, in some cases, be conclusive in determining that the estimated cash flows of the entity are expected to significantly change as a result of the exchange.

**Applying the Basic Principle**

30-8 Fair value should be regarded as not determinable within reasonable limits if major uncertainties exist about the realizability of the value that would be assigned to an asset received in a nonmonetary transaction accounted for at fair value. An exchange involving parties with essentially opposing interests is not considered a prerequisite to determining a fair value of a nonmonetary asset transferred; nor does an exchange ensure that a fair value for accounting purposes can be ascertained within reasonable limits. If neither the fair value of a nonmonetary asset transferred nor the fair value of a nonmonetary asset received in exchange is determinable within reasonable limits, the recorded amount of the nonmonetary asset transferred from the entity may be the only available measure of the transaction.
ASC 845-10-30-2 states that “[i]f one of the parties in a nonmonetary transaction could have elected to receive cash instead of the nonmonetary asset, the amount of cash that could have been received may be evidence of the fair value of the nonmonetary assets exchanged.” The cash that could have been received in lieu of the nonmonetary asset exchanged may constitute evidence of fair value; however, it should not be considered a substitute for, or an expedient way of determining, fair value. The initial fair value measurement of the nonmonetary asset exchanged should be determined in accordance with ASC 820.

10.10.17 Reorganizations

10.10.17.1 General

<table>
<thead>
<tr>
<th>ASC 852-20</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>30-2</strong> A write-down of assets below amounts that are likely to be subsequently realized, though it may result in conservatism in the balance sheet at the readjustment date, may also result in overstatement of earnings or of retained earnings when the assets are subsequently realized. Therefore, in general, assets shall be carried forward as of the date of readjustment at fair and not unduly conservative amounts, determined with due regard for the accounting to be subsequently employed by the entity.</td>
</tr>
<tr>
<td><strong>30-3</strong> If the fair value of any asset is not readily determinable a conservative estimate may be made, but in that case the amount shall be described as an estimate. Paragraph 852-20-35-2 describes the subsequent accounting for any material difference arising through realization or otherwise and not attributable to events occurring or circumstances arising after that date.</td>
</tr>
</tbody>
</table>

**General**

**35-2** If the fair value of any asset was not readily determinable and a conservative estimate was made at the date of the readjustment, any material difference arising through realization or otherwise and not attributable to events occurring or circumstances arising after that date shall not be carried to income or retained earnings. Similarly, if provisions for losses or charges established at the date of readjustment are subsequently found to have been excessive or insufficient, the difference shall not be carried to retained earnings nor used to offset losses or gains originating after the readjustment, but shall be recorded as additional paid-in capital.

**SEC Staff Accounting Bulletin**

SAB Topic 5.S, Quasi-Reorganization [Reproduced in ASC 852-20-S99-2]

**Question 3:** In connection with a quasi-reorganization, may there be a write-up of net assets?

**Interpretive Response:** No. The staff believes that increases in the recorded values of specific assets (or reductions in liabilities) to fair value are appropriate providing such adjustments are factually supportable, however, the amount of such increases are limited to offsetting adjustments to reflect decreases in other assets (or increases in liabilities) to reflect their new fair value. In other words, a quasi-reorganization should not result in a write-up of net assets of the registrant.
10.10.17.2 Determining Fair Value of Net Assets in a Quasi-Reorganization

ASC 852-20-30-2 and 30-3 provide guidance on the valuation of assets (and liabilities) in a quasi-reorganization. In a quasi-reorganization, an entity's assets and liabilities (net assets) should be remeasured to fair value. Generally, an entity should calculate the fair value of net assets the same way it measures assets acquired and liabilities assumed in a business combination, as described in ASC 805-20-25 and ASC 805-20-30. (See Section 2.3.6.1 for a discussion of exceptions to applying the guidance in ASC 805-20-25 and ASC 805-20-30.) In addition, disposition of an asset shortly after a quasi-reorganization (e.g., generally within one year) serves as persuasive evidence of the value of the asset as of the date of the quasi-reorganization unless a significant event validates a change in the value of the asset in the intervening period.

Accordingly, some assets may be written up and others may be written down in value. However, the quasi-reorganization adjustments in total must not result in a write-up of net assets. If the calculated fair value adjustments would result in a write-up of net assets, the entity should first reduce goodwill, then other intangible assets, and then other noncurrent assets until the adjustment of net assets equals zero.

10.10.17.2.1 Determining Fair Value of Inventories

As discussed in Section 10.10.17.2 above, the process for calculating the fair value of an entity's net assets in a quasi-reorganization should generally be the same as that for adjusting assets and liabilities to fair value in a business combination. ASC 805-20-30-1 requires that finished goods and works-in-process inventories be measured at fair value. However, the guidance in ASC 805-20-30-1 should not necessarily be used to value inventories in a quasi-reorganization. An entity effecting a quasi-reorganization may either use the approach in ASC 805-20-30-1 or value its inventories on the basis of replacement costs. The replacement-costs valuation technique is appropriate for inventories because the entity is a continuing entity that, in fact, manufactured the inventories in question.

10.10.17.3 Impact of Quasi-Reorganization Fair Value Adjustments on Impairment Testing

ASC 360-10-35-21 states that “[a] long-lived asset (asset group) shall be tested for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable.” An impairment loss that would result from such an evaluation is treated differently than a fair value adjustment recognized in a quasi-reorganization. An entity must use significant judgment in determining whether an asset is impaired when a fair value write-down would otherwise be made in a quasi-reorganization. When an asset impairment, rather than an adjustment of fair value, is recorded in a quasi-reorganization, impairment losses are reflected in the statement of operations for the period before the effective date of the reorganization and fair value adjustments in a quasi-reorganization are reflected as direct entries to the accumulated deficit. A pending quasi-reorganization should be regarded as an impairment indicator and, accordingly, impairment should be assessed immediately before the effective date of the reorganization.
10.10.18 Transfers and Servicing

**ASC 860-20**

*Estimating the Fair Value of Certain Beneficial Interests*

55-16 Trust liquidation methods that allocate receipts of principal or interest between beneficial interest holders and transferees in proportions different from their stated percentage of ownership interests do not affect whether the transferor should obtain sale accounting and derecognize those transferred assets, assuming the trust is not required to be consolidated by the transferor. However, both turbo and bullet provisions in securitization structures (as discussed in paragraph 860-10-05-3) should be taken into consideration in determining the fair values of assets obtained by the transferor and transferee.

**ASC 860-50**

30-1 An entity shall initially measure at fair value, a servicing asset or servicing liability that qualifies for separate recognition regardless of whether explicit consideration was exchanged.

30-2 Typically, the benefits of servicing are expected to be more than adequate compensation to a servicer for performing the servicing, and the contract results in a servicing asset. However, if the benefits of servicing are not expected to adequately compensate a servicer for performing the servicing, the contract results in a servicing liability. Paragraph 860-50-35-1A states that a servicing asset may become a servicing liability, or vice versa, if circumstances change. The initial measure for servicing may be zero if the benefits of servicing are just adequate to compensate the servicer for its servicing responsibilities. A servicing contract that entitles the servicer to receive benefits of servicing just equal to adequate compensation, regardless of the servicer’s own servicing costs, does not result in recognizing a servicing asset or a servicing liability. A purchaser would neither pay nor receive payment to obtain the right to service for a rate just equal to adequate compensation.

30-3 The determination of whether the servicer is adequately compensated for servicing specified assets is based on the amount demanded by the marketplace, not the contractual amount to be paid to a replacement servicer. However, that contractual provision would be relevant for determining the amount of contractually specified servicing fees. Therefore, the amount that would be paid to a replacement servicer under the terms of the servicing contract can be more or less than adequate compensation.

30-4 Whether a servicing asset or servicing liability is recorded is a function of the marketplace, not the servicer’s cost of servicing. For example, a loss shall not be recognized if a servicing fee that is equal to or greater than adequate compensation is to be received but the servicer’s anticipated cost of servicing would exceed the fee.

30-6 When valuing the right to receive future cash flows from ancillary sources such as late fees, an entity shall estimate the value of the right to benefit from the cash flows of potential future transactions, not the value of the expected cash flows to be derived from future transactions.

30-7 Entities shall consider the nature of the assets being serviced as a factor in determining the fair value of a servicing asset or servicing liability. The types of assets being serviced affect the amount required to adequately compensate the servicer. Several variables, including the nature of the underlying assets, shall be considered in determining whether a servicer is adequately compensated. For example, the amount of effort required to service a home equity loan likely would be different from the amount of effort required to service a credit card receivable or a small business administration loan.
In initially recognizing an asset for a servicing right (or a liability for a servicing obligation) under ASC 860-50, an entity must compare the (1) estimated future revenues from contractually specified servicing fees, late charges, and other ancillary revenues (benefits of servicing) with (2) adequate compensation. The concept of “adequate compensation” focuses on the benefits that fairly compensate a substitute servicer if one is required, including the profit that would be demanded in the marketplace. Since adequate compensation is determined in the marketplace, a servicer’s internal costs of servicing financial assets do not factor into the determination of the fair value of servicing assets or liabilities.

The cost of servicing financial assets varies among servicers and depends on factors such as the volume of financial assets serviced, the geographic location of the servicer, and the efficiency of the servicer. Accordingly, a servicer’s own cost of servicing financial assets is not relevant in the determination of adequate compensation. The determination of adequate compensation in an illiquid market often involves significant analysis and should be well documented. Adequate compensation is also discussed in ASC 860-50-30-2 through 30-7.

The approach in ASC 860 is consistent with the guidance in ASC 820, emphasizing that fair value measurement is market-based, not entity-specific. Therefore, a fair value measurement would also be determined on the basis of assumptions that market participants would use in pricing the servicing asset or liability.

### 10.10.19 Industry Guidance

#### 10.10.19.1 ASC 926, Entertainment — Films

<table>
<thead>
<tr>
<th>ASC 926-20</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Film Costs Valuation</strong></td>
</tr>
<tr>
<td><strong>35-14</strong> A discounted cash flows model is often used to estimate fair value. If applicable, future cash flows based on the terms of any existing contractual arrangements, including cash flows over existing license periods without consideration of the limitations set forth in paragraphs 926-20-35-5 and 926-20-35-11, shall be included.</td>
</tr>
</tbody>
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<table>
<thead>
<tr>
<th><strong>Pending Content (Transition Guidance: ASC 926-20-65-2)</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>35-14</strong> A discounted cash flow model may be used to estimate fair value. If applicable, future cash flows based on the terms of any existing contractual arrangements, including cash flows over existing license periods without consideration of the limitations set forth in paragraph 926-20-35-5, shall be included.</td>
</tr>
</tbody>
</table>

**35-15** An entity shall consider the following factors, among others, in estimating future cash inflows for a film:

a. If previously released, the film’s performance in prior markets
b. The public’s perception of the film’s story, cast, director, or producer
c. Historical results of similar films
d. Historical results of the cast, director, or producer on prior films
e. Running time of the film.

In determining a film’s fair value, it is also necessary to consider those cash outflows necessary to generate the film’s cash inflows. Therefore, an entity shall incorporate, if applicable, its estimates of future costs to complete a film, future exploitation and participation costs, or other necessary cash outflows in its determination of fair value when using a discounted cash flows model.
ASC 926-20 (continued)

Pending Content (Transition Guidance: ASC 926-20-65-2)

35-15 An entity shall consider the following factors, among others, in estimating future cash inflows for a film:
   a. If previously released, the film's performance in prior markets
   b. The public's perception of the film's story, cast, director, or producer
   c. Historical results of similar films
   d. Historical results of the cast, director, or producer on prior films
   e. Running time of the film.

In determining a film's (or film group's) fair value, it is also necessary to consider those cash outflows necessary to generate the film's (or film group's) cash inflows. Therefore, an entity shall incorporate, if applicable, its estimates of future costs to complete a film, future exploitation and participation costs, or other necessary cash outflows in its determination of fair value when using a discounted cash flow model.

35-16 When using the traditional discounted cash flow approach to estimate the fair value of a film, the relevant future cash inflows and outflows shall represent the entity's estimate of the most likely cash flows. When determining the fair value of a film using the expected cash flows approach, all possible relevant future cash inflows and outflows shall be probability-weighted by period and the estimated mean or average by period shall be used.

Pending Content (Transition Guidance: ASC 926-20-65-2)

35-16 When using the traditional discounted cash flow approach to estimate the fair value of a film (or film group), the relevant future cash inflows and outflows shall represent the entity's estimate of the most likely cash flows. When determining the fair value of a film (or film group) using the expected cash flow approach, all possible relevant future cash inflows and outflows shall be probability-weighted by period and the estimated mean or average by period shall be used.

35-17 When determining the fair value of a film using a traditional discounted cash flow approach, the discount rate(s) shall not be an entity's incremental borrowing rate(s), liability settlement rate(s), or weighted average cost of capital because those rates typically do not reflect the risks associated with a particular film. The discount rate(s) shall consider the time value of money and the expectations about possible variations in the amount or timing of the most likely cash flows and an element to reflect the price market participants would seek for bearing the uncertainty inherent in such an asset, as well as other factors, sometimes unidentifiable, including illiquidity and market imperfections. When determining the fair value of a film using the expected cash flow approach, the discount rate(s) also would consider the time value of money. Because they are reflected in the expected cash flows, there would be no adjustment for possible variations in the amounts or timing of those cash flows. If not reflected in risk-adjusted expected cash flows, an additional element to reflect the price market participants would seek for bearing the uncertainty inherent in such an asset as well as other factors, sometimes unidentifiable, including illiquidity and market imperfections, shall be added to the discount rate(s).
Chapter 10 — Subsequent Measurement

ASC 926-20 (continued)

Pending Content (Transition Guidance: ASC 926-20-65-2)

35-17 When determining the fair value of a film (or film group) using a traditional discounted cash flow approach, the discount rate(s) shall not be an entity’s incremental borrowing rate(s), liability settlement rate(s), or weighted average cost of capital because those rates typically do not reflect the risks associated with a particular film (or film group). The discount rate(s) shall consider the time value of money and the expectations about possible variations in the amount or timing of the most likely cash flows and an element to reflect the price market participants would seek for bearing the uncertainty inherent in such an asset, as well as other factors, sometimes unidentifiable, including illiquidity and market imperfections. When determining the fair value of a film (or film group) using the expected cash flow approach, the discount rate(s) also would consider the time value of money. Because they are reflected in the expected cash flows, there would be no adjustment for possible variations in the amounts or timing of those cash flows. If not reflected in risk-adjusted expected cash flows, an additional element to reflect the price market participants would seek for bearing the uncertainty inherent in such an asset as well as other factors, sometimes unidentifiable, including illiquidity and market imperfections, shall be added to the discount rate(s).

Film Properties

40-3 An entity shall measure the loss as the amount by which the carrying amount of the project exceeds its fair value. Unless management, having the authority to approve the action, has committed to a plan to sell such property, the rebuttable presumption is that the entity will abandon the property and, as such, its fair value shall be zero.

10.10.19.2 ASC 930, Extractive Activities

ASC 930-805

Value Beyond Proven and Probable Reserves

30-1 An entity shall include value beyond proven and probable reserves in the value allocated to mining assets in a purchase price allocation to the extent that a market participant would include value beyond proven and probable reserves in determining the fair value of the asset.

Anticipated Future Price Fluctuations

30-2 An entity shall include the effects of anticipated fluctuations in the future market price of minerals in determining the fair value of mining assets in a purchase price allocation in a manner that is consistent with the expectations of marketplace participants. Generally, an entity should consider all available information including current prices, historical averages, and forward pricing curves. Those marketplace assumptions typically should be consistent with the acquiring entity’s operating plans with respect to developing and producing minerals. It generally would be inappropriate for an entity to use a single factor, such as the current price or a historical average, as a surrogate for estimating future prices without considering other information that a market participant would consider.
10.10.19.3  ASC 940, Financial Services — Brokers and Dealers

<table>
<thead>
<tr>
<th>ASC 940-820</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>30-1</strong> This Section does not purport to delineate all factors that may be considered by management in determining the fair value assigned to a particular financial instrument. However, the following is a list of certain factors that have been taken into consideration by broker-dealers as part of the determination of fair value:</td>
</tr>
<tr>
<td>a. Financial standing of the issuer</td>
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<tr>
<td>b. Business and financial plan of the issuer</td>
</tr>
<tr>
<td>c. Cost at date of purchase</td>
</tr>
<tr>
<td>d. The liquidity of the market</td>
</tr>
<tr>
<td>e. Contractual restrictions on salability</td>
</tr>
<tr>
<td>f. Pending public offering with respect to the financial instrument</td>
</tr>
<tr>
<td>g. Pending reorganization activity affecting the financial instrument (such as merger proposals, tender offers, debt restructurings, and conversions)</td>
</tr>
<tr>
<td>h. Reported prices and the extent of public trading in similar financial instruments of the issuer or comparable entities</td>
</tr>
<tr>
<td>i. Ability of the issuer to obtain needed financing</td>
</tr>
<tr>
<td>j. Changes in the economic conditions affecting the issuer</td>
</tr>
<tr>
<td>k. A recent purchase or sale of a security of the entity</td>
</tr>
<tr>
<td>l. Pricing by other dealers in similar securities.</td>
</tr>
</tbody>
</table>

See also Sections 9.2 and 10.10.2.

10.10.19.4  ASC 942, Financial Services — Depository and Lending

<table>
<thead>
<tr>
<th>ASC 942-310</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Debt-Equity Swap Programs</strong></td>
</tr>
<tr>
<td><strong>30-2</strong> Since the secondary market for debt of financially troubled countries may be considered to be thin, it may not be the best indicator of the fair value of the equity investment or of net assets received. In light of this thin secondary market and of the unique nature of the transaction, it is also necessary to examine the fair value of the equity investment or net assets received. In arriving at the fair value of a debt-equity swap, both the secondary market price of the loan given up and the fair value of the equity investment or net assets received shall be considered.</td>
</tr>
<tr>
<td><strong>30-3</strong> It is the responsibility of management to measure fair value considering all of the circumstances and to see that the measurement of fair value is based on reasonable methods and assumptions consistent with Topic 820, including, as needed, information from independent appraisals. Factors to consider in measuring fair values include the following:</td>
</tr>
<tr>
<td>a. Similar transactions for cash</td>
</tr>
<tr>
<td>b. Estimated cash flows from the equity investment or net assets received</td>
</tr>
<tr>
<td>c. Fair value of similar equity investments, if any</td>
</tr>
<tr>
<td>d. Currency restrictions, if any, affecting dividends, the sale of the investment, or the repatriation of capital.</td>
</tr>
</tbody>
</table>
**Chapter 10 — Subsequent Measurement**

**ASC 942-470**

**Fair Value of Deposit Liabilities**

50-1 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.

**10.10.19.5 ASC 944, Financial Services — Insurance**

**ASC 944-40**

**Pending Content (Transition Guidance: ASC 944-40-65-2)**

**Discount Rate**

55-13E An insurance entity should maximize the use of current observable market prices of upper-medium-grade (low-credit-risk) fixed-income instruments with durations similar to the liability for future policy benefits.

a. An insurance entity should not substitute its own estimates for observable market data unless the market data reflect transactions that are not orderly (see paragraphs 820-10-35-54I through 35-54J for additional guidance on determining whether transactions are not orderly).

b. In determining points on the yield curve for which there are limited or no observable market data for upper-medium-grade (low-credit-risk) fixed-income instruments, an insurance entity should use an estimate that is consistent with existing guidance on fair value measurement in Topic 820, particularly for Level 3 fair value measurement.

**10.10.19.6 ASC 946, Financial Services — Investment Companies**

**ASC 946-320**

**Dividends**

35-6 Stock splits and stock dividends in shares of the same class as the shares owned are not income to the investment company. However, dividends for which the recipient has the choice to receive cash or stock are usually recognized as investment income in the amount of the cash option, because in such cases cash is usually the best evidence of fair value of the stock.


**ASC 946-830**

**Purchased Interest**

45-14 Purchased interest represents the interest accrued between the last coupon date and the settlement date of the purchase. It should be recorded in the functional currency as interest receivable at the spot rate on the purchase trade date, and subsequently measured at fair value using each valuation date’s spot rate. After the settlement date, daily interest income should be accrued at the daily spot rate. It may be impractical to prepare the foregoing calculations daily, and, therefore, the use of a weekly or monthly average rate may be appropriate in many cases, especially if the exchange rate does not fluctuate significantly. However, if the exchange rate fluctuation is significant, the calculation should be made daily.
ASC 946-830 (continued)

**Subsequently Measuring at Fair Value**

45-16 The fair value of securities shall initially be determined in the foreign currency and translated at the spot rate on the purchase trade date. The unrealized gain or loss between the original cost (translated on the trade date) and the fair value (translated on the valuation date) comprises both of the following elements:

a. Changes in the fair value of securities before translation

b. Movement in foreign currency rate.

10.10.19.7 **ASC 948, Financial Services — Mortgage Banking**

**ASC 948-310**

**Loans Held for Sale**

35-3 The fair value of mortgage loans and mortgage-backed securities held for sale shall be measured by type of loan. At a minimum, the fair value of residential (one- to four-family dwellings) and commercial mortgage loans shall be measured separately. Either the aggregate or individual loan basis may be used in determining the lower of cost or fair value for each type of loan. Fair value for loans subject to investor purchase commitments (committed loans) and loans held on a speculative basis (uncommitted loans) shall be measured separately as follows:

a. Committed loans. Mortgage loans covered by investor commitments shall be based on the fair values of the loans.

b. Uncommitted loans. Fair value for uncommitted loans shall be based on principal market or, in the absence of a principal market, in the most advantageous market (see paragraphs 820-10-35-5 through 35-6C). That determination relies on the principles in Topic 820 and would include consideration of the following:

1. Market prices and yields sought by market participants in the principal or most advantageous market

2. Quoted Government National Mortgage Association (GNMA) security prices or other public market quotations for long-term mortgage loan rates

3. Federal Home Loan Mortgage Corporation (FHLMC) and Federal National Mortgage Association (FNMA) current delivery prices.

**Pending Content (Transition Guidance: ASC 326-10-65-1)**

35-3 The fair value of mortgage loans and mortgage-backed securities held for sale shall be measured by type of loan. At a minimum, the fair value of residential (one- to four-family dwellings) and commercial mortgage loans shall be measured separately. Either the aggregate or individual loan basis may be used in determining the lower of amortized cost basis or fair value for each type of loan. Fair value for loans subject to investor purchase commitments (committed loans) and loans held on a speculative basis (uncommitted loans) shall be measured separately as follows:

a. Committed loans. Mortgage loans covered by investor commitments shall be based on the fair values of the loans.

b. Uncommitted loans. Fair value for uncommitted loans shall be based on principal market or, in the absence of a principal market, in the most advantageous market (see paragraphs 820-10-35-5 through 35-6C). That determination relies on the principles in Topic 820 and would include consideration of the following:

1. Market prices and yields sought by market participants in the principal or most advantageous market

2. Quoted Government National Mortgage Association (GNMA) security prices or other public market quotations for long-term mortgage loan rates

3. Federal Home Loan Mortgage Corporation (FHLMC) and Federal National Mortgage Association (FNMA) current delivery prices.
Other Considerations

35-6 Capitalized costs of acquiring rights to service mortgage loans, associated with the purchase or origination of mortgage loans (see paragraph 860-50-25-1), shall be excluded from the cost of mortgage loans for the purpose of determining the lower of cost or fair value.

10.10.19.8 ASC 958, Not-for-Profit Entities

ASC 958-30

Fair Value Measurement

30-1 Topic 820 establishes a framework for measuring fair value. This Subtopic uses present value techniques as one possible technique to measure the contribution revenue and obligation to other beneficiaries of a split-interest agreement. See paragraphs 820-10-55-4 through 55-20 for implementation guidance for using present value techniques if the measurement objective is fair value. Other valuation techniques are also available, as discussed in Section 820-10-35.

Split-Interest Agreements Other Than Pooled Income Funds or Net-Income Unitrusts

30-5 If the split-interest agreement is other than a pooled income fund or net income unitrust (for example, a charitable gift annuity, a charitable lead trust, or a charitable remainder trust), the transferred assets, or a portion of those assets, are being held for the benefit of others, such as the donor or third parties designated by the donor. That liability shall be measured at fair value at the date of initial recognition. If present value techniques are used to measure fair value, the liability is measured at the present value of the future payments to be made to the other beneficiaries.

30-6 Any present value technique for measuring the fair value of the contribution or payments to be made to other beneficiaries shall consider the elements described in paragraph 820-10-55-5, including the following:

   a. The estimated return on the invested assets during the expected term of the agreement
   b. The contractual payment obligations under the agreement
   c. A discount rate commensurate with the risks involved.

30-7 Under a lead interest agreement, the fair value of the contribution can be estimated directly based on the present value of the future distributions to be received by the NFP as a beneficiary. Under lead interest agreements, the future payments to be made to other beneficiaries will be made by the NFP only after the NFP receives its benefits. In those situations, the present value of the future payments to be made to other beneficiaries may be estimated by the fair value of the assets contributed by the donor under the agreement less the fair value of the benefits to be received by the NFP. If present value techniques are used, the fair value of the benefits to be received by the NFP shall be measured at the present value of the benefits to be received over the expected term of the agreement.

30-8 Under remainder interest agreements, the present value of the future payments to be made to other beneficiaries can be estimated directly based on the terms of the agreement. Future distributions will be received by the NFP only after obligations to other beneficiaries are satisfied. In those cases, the fair value of the contribution may be estimated based on the fair value of the assets contributed by the donor less the fair value of the payments to be made to other beneficiaries.
Pooled Income Funds or Net-Income Unitrusts

30-10 The contributed assets received from the donor under a pooled income fund agreement or a net income unitrust shall be recognized at fair value. The contribution shall be measured at fair value. Present value techniques are one valuation technique for measuring the fair value of the contribution; other valuation techniques are also available, as described in Topic 820. If present value techniques are used, the contribution may be measured at the fair value of the assets to be received, discounted for the estimated time period until the donor's death.

Fair Value Measurement

35-1 Topic 820 establishes a framework for measuring fair value. This Subtopic uses present value techniques as one possible technique to measure the obligation to other beneficiaries of a split-interest agreement. See paragraphs 820-10-55-4 through 55-20 for implementation guidance for using present value techniques if the measurement objective is fair value.

35-2 The measurement objective is fair value for the following split-interest obligations:
   a. Embedded derivatives subject to the measurement provisions of Topic 815
   b. Obligations for which the not-for-profit entity (NFP) elects the fair value option pursuant to the Fair Value Option Subsections of Subtopic 825-10
   c. Obligations containing embedded derivatives that the NFP has irrevocably elected to measure in their entirety at fair value in conformity with Section 815-15-25.

Additionally, in circumstances in which cash or other assets contributed by donors under split-interest agreements are held by independent trustees, such as a charitable trust for which a bank is a trustee, or by other fiscal agents of the donors or otherwise not controlled by the NFP, the measurement objective for the beneficial interest in periods after the period of initial recognition is fair value.

35-3 In circumstances in which the fair value is measured at the present value of the future cash flows, all elements discussed in paragraph 820-10-55-5, including discount rate assumptions, shall be revised at each measurement date to reflect current market conditions.

Split-Interest Agreements With Embedded Derivatives

35-7 If an NFP does not elect to report a split-interest obligation at fair value as described in paragraph 958-30-35-2, a split-interest obligation with an embedded derivative is bifurcated into its debt host contract and embedded derivative. The debt host contract is the liability for the payment to the beneficiary that would be required if the fair value of the trust assets does not change over the specified period. The embedded derivative represents the liability (or contrariability) for the increase (or decrease) in the payments to the beneficiary due to changes in the fair value of the trust assets over the specified period. In circumstances in which the liability is measured using present value techniques, the discount rate assumptions on the debt host contract shall not be revised after initial recognition, consistent with the preceding paragraph. In accordance with paragraph 815-10-35-1, the embedded derivative is subsequently measured at fair value. If the fair value of the embedded derivative is measured using present value techniques, all elements discussed in paragraph 820-10-55-5, including the discount rate assumptions on the embedded derivative, shall be revised at each measurement date to reflect current market conditions.

35-8 In conformity with paragraph 815-15-25-53, if an NFP cannot reliably identify and measure the embedded derivative, the entire split-interest liability shall be measured at fair value (that is, all elements discussed in paragraph 820-10-55-5, including discount rate assumptions, shall be revised to reflect current market conditions).
Chapter 10 — Subsequent Measurement

ASC 958-30 (continued)

Assets Held by a Third Party

35-10 Pursuant to paragraph 958-605-35-3, if an NFP is the beneficiary of a split-interest agreement held by a third party and has an unconditional right to receive all or a portion of the specified cash flows from the assets held pursuant to that agreement, the NFP shall subsequently remeasure that beneficial interest at fair value. Changes in the fair value of the beneficial interest shall be recognized in the statement of activities. The change in the value of split-interest agreements is the change in the fair value of the NFP's beneficial interest, which shall be determined using the same valuation technique that was used to measure the asset initially. Distributions from the trust shall be reflected as a reduction in the beneficial interest.

ASC 958-310

Fair Value Measurement

35-1 The Fair Value Option Subsections of Subtopic 825-10 create a fair value option under which a not-for-profit entity (NFP) may irrevocably elect fair value as the initial and subsequent measure for most receivables. If an NFP elects to measure a receivable at fair value and uses a present value technique to measure fair value, the discount rate assumptions, and all other elements discussed in paragraph 820-10-55-5 shall be revised at each measurement date to reflect current market conditions. Paragraph 820-10-35-2B states that a fair value measurement takes into account the effect of a restriction on the sale or use of an asset if market participants would take into account the effect of the restriction when pricing the asset. Example 6 (see paragraph 820-10-55-51) illustrates that restrictions that are a characteristic of an asset and, therefore, would transfer to a market participant are the only restrictions reflected in fair value. Donor restrictions that are specific to the donee are reflected in the classification of net assets, not in the measurement of fair value.

Changes in the Fair Value of Underlying Noncash Assets — Gifts of Certain Securities

35-11 The value of a contribution receivable arising from an unconditional promise to give equity securities with readily determinable fair values or debt securities may change between the date the unconditional promise to give is recognized and the date the asset promised is received because of changes in the future fair value of the underlying securities. For purposes of subsequent measurement, the method of determining the future fair value of the underlying securities shall be the same as the method used for determining that amount for purposes of initial measurement. Thus, if a promise to give securities is measured based on the fair value of the underlying securities at the date of gift, as described in paragraph 958-605-30-8, an observed change in the current fair value of the underlying securities shall be recognized. The change shall be reported as an increase or a decrease in contribution revenue in the period(s) in which the change occurs. The change shall be recognized in the net asset class in which the contribution was originally reported or in the net asset class in which the net assets are represented.

Changes in the Fair Value of Underlying Noncash Assets — Gifts of Other Assets

35-12 The value of a contribution receivable arising from an unconditional promise to give noncash assets other than equity securities with readily determinable fair values or debt securities may change between the date the unconditional promise to give is recognized and the date the asset promised is received because of changes in the future fair value of the underlying noncash assets. For purposes of subsequent measurement, the method for determining the future fair value of the underlying noncash asset shall be the same as the method used for determining that amount for purposes of initial measurement. Accordingly, assumed relationships, such as the relationship between the market price of the noncash asset at the time the initial measurement is made and its projected market price at the date the asset is expected to be received, shall be presumed to continue in determining whether the future fair value of the underlying noncash asset has changed.
ASC 958-405

Liability for Promises to Give

35-1 If the present value of the amounts to be paid is used to measure fair value of an unconditional promise to give at initial recognition, in conformity with paragraphs 835-30-25-10 through 25-11, the discount rate shall be determined at the time the unconditional promise to give is initially recognized and shall not be revised, unless the promise to give is subsequently remeasured at fair value pursuant to the Fair Value Option Subsections of Subtopic 825-10.

ASC 958-605

30-3 Paragraph 820-10-35-2B states that a fair value measurement takes into account the effect of a restriction on the sale or use of an asset if market participants would take into account the effect of the restriction when pricing the asset. Example 6 (see paragraph 820-10-55-51) illustrates that restrictions that are a characteristic of an asset, and, therefore, would transfer to a market participant, are the only restrictions reflected in fair value. Donor restrictions that are specific to the donee are reflected in the classification of net assets, not in the measurement of fair value.

Unconditional Promises to Give

30-4 If present value techniques are used to measure the fair value of unconditional promises to give, the entity shall determine the amount and timing of the future cash flows of unconditional promises to give cash (or, for promises to give noncash assets, the quantity and nature of assets expected to be received). In making that determination, the entity shall consider all the elements in paragraph 820-10-55-5, including the following:

a. When the receivable is expected to be collected
b. The creditworthiness of the other parties
c. The entity's past collection experience
d. The entity's policies concerning the enforcement of promises to give
e. Expectations about possible variations in the amount or timing of the cash flows (that is, the uncertainty inherent in the cash flows)
f. Other factors concerning the receivable's collectibility.

30-5 If present value techniques are used to measure fair value, the present value of unconditional promises to give should be measured using a discount rate that is consistent with the general principles for present value measurement discussed in paragraphs 820-10-55-5 through 55-9. In conformity with paragraph 835-30-25-11, the discount rate shall be determined at the time the unconditional promise to give is initially recognized and shall not be revised subsequently unless the entity has elected to measure the promise to give at fair value in conformity with the Fair Value Option Subsections of Subtopic 825-10.

30-6 Unconditional promises to give that are expected to be collected in less than one year may be measured at net realizable value because that amount results in a reasonable estimate of fair value.

30-7 If a promise to give has not previously been recognized as contribution revenue because it was conditional, fair value shall be measured when the conditions are met.
Unconditional Promises to Give Noncash Assets

30-8 A present value technique is one valuation technique for measuring the fair value of an unconditional promise to give noncash assets; other valuation techniques also are available, as described in Topic 820. If present value techniques are used, the fair value of contributions arising from unconditional promises to give noncash assets might be determined based on the present value of the projected fair value of the underlying noncash assets at the date that those assets are expected to be received (that projected fair value is referred to in this Section as the future fair value) and in the quantities that those assets are expected to be received, if the date is one year or more after the financial statement date. Both the likelihood of the promise being fulfilled and the future fair value of those underlying assets, such as the future fair value per share of a promised equity security, should be considered in determining the future amount to be discounted. The quantity, nature, and timing of assets expected to be received, such as the number of shares of a promised equity security, the entity in which those shares represent an equity interest, and when those shares will be received should be considered in determining the likelihood of the promise being fulfilled. In cases in which the future fair value of the underlying asset is difficult to determine, the fair value of an unconditional promise to give noncash assets may be based on the fair value of the underlying asset at the date of initial recognition. No discount for the time value of money shall be reported if an asset’s fair value at the date of initial recognition is used to measure the fair value of the contribution.

Inventory Items

30-9 Inputs for measuring fair value of contributed inventory items may be obtained from published catalogs, vendors, independent appraisals, and other sources. If methods such as estimates, averages, or computational approximations, such as average value per pound or subsequent sales, can reduce the cost of measuring the fair value of inventory, use of those methods is appropriate, provided the methods are applied consistently, and the results of applying those methods are reasonably expected not to be materially different from the results of a detailed measurement of the fair value of contributed inventory.

Contributed Services

30-10 Contributions of services that create or enhance nonfinancial assets may be measured by referring to either the fair value of the services received or the fair value of the asset or of the asset enhancement resulting from the services. Fair value should be used for the measure regardless of whether the NFP could afford to purchase the services at their fair value.

Gifts in Kind

30-11 Gifts in kind that can be used or sold shall be measured at fair value. In determining fair value, entities should consider the quality and quantity of the gifts, as well as any applicable discounts that would have been received by the entity, including discounts based on that quantity if the assets had been acquired in exchange transactions. Fair value would generally not increase when a gift in kind is passed from one entity to another. However, fair value could increase if an entity adds value to the gift, such as by cleaning and packaging the gift. Any increases should be evaluated to determine whether the entity did, in fact, add to the fair value of the assets.

Specified Beneficiary

30-14 If the beneficiary has an unconditional right to receive all or a portion of the specified cash flows from a charitable trust or other identifiable pool of assets, the beneficiary shall measure that beneficial interest at fair value. The fair value of a perpetual trust held by a third party generally can be measured using the fair value of the assets contributed to the trust, unless facts and circumstances indicate that the fair value of the beneficial interest differs from the fair value of the assets contributed to the trust. If the beneficiary recognizes a receivable pursuant to paragraph 958-605-25-30, the beneficiary shall measure its rights to the assets held by a recipient entity at fair value in accordance with paragraph 958-605-30-2 and paragraphs 958-605-30-4 through 30-7 for unconditional promises to give.
Specified Beneficiary

35-3 If the beneficiary has an unconditional right to receive all or a portion of the specified cash flows from a charitable trust or other identifiable pool of assets, the beneficiary shall subsequently remeasure that beneficial interest at fair value (see paragraph 958-30-35-10). The fair value of a perpetual trust held by a third party generally can be measured using the fair value of the assets of the trust at the date of remeasurement, unless facts and circumstances indicate that the fair value of the beneficial interest differs from the fair value of the assets contributed to the trust. Annual distributions from a perpetual trust held by a third party are reported as investment income.

Example 1: Contribution of Real Property

55-34 Mission A would recognize the contributed property as an asset and as support and measure that property at its fair value (see paragraph 958-605-30-2). Information necessary to estimate the fair value of that property could be obtained from various sources, including amounts recently paid for similar properties in the locality, and estimates of its replacement cost adjusted to reflect the price that would be received for the contributed property. This contribution is revenue without donor restrictions because the donated assets may be used for any purpose and the donor did not impose a time restriction.

Example 4: Contribution of Utilities

55-44 The simultaneous receipt and use of electricity or other utilities is a form of contributed assets and not services. Foundation D would recognize the fair value of the contributed electricity as both revenue and expense in the period it is received and used (see paragraph 958-605-30-2). Foundation D could estimate the fair value of the electricity received by using rates normally charged to a consumer of similar usage requirements.

Example 7: Contribution of Services to Construct a Building

55-54 Institute G would recognize the services contributed by the construction entity because the contributed services received meet the condition in paragraph 958-605-25-16(a) (the services received create or enhance nonfinancial assets) or because the services meet the condition in paragraph 958-605-25-16(b) (the services require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation). Contributions of services that create or enhance nonfinancial assets may be measured by referring to either the fair value of the services received or the fair value of the asset or of the asset enhancement resulting from the services (see paragraph 958-605-30-10). In this Example, the fair value of the contributed services received could be determined by subtracting the cost of the purchased services, materials, and permits ($400,000) from the fair value of the asset created ($725,000), which results in contributed services received of $325,000. Alternatively, the amount the construction entity would have charged could be used if more readily available.

Example 8: Contribution of Teaching Services

55-58 University H would recognize both revenue and expense for the services contributed by the uncompensated faculty members because the contribution meets the condition in paragraph 958-605-25-16(b). Teaching requires specialized skills; the religious personnel are qualified and trained to provide those skills; and University H typically would hire paid instructors if the religious personnel did not donate their services. University H could refer to the salaries it pays similarly qualified compensated faculty members to determine fair value of the services received.

Similarly, if the uncompensated faculty members were given a nominal stipend to help defray certain of their out-of-pocket expenses, University H still would recognize both revenue and expense for the services contributed. The contribution received would be measured at the fair value of the services received less the amount of the nominal stipend paid.
Example 7: Donor Establishes a Charitable Trust

The Contribution Received Subsections of this Subtopic do not establish standards for the trustee, National Bank J (see paragraph 958-605-15-9). Because Museum I is unable to influence the operating or financial decisions of the trustee, Museum I and National Bank are not financially interrelated entities. Therefore, Museum I would recognize its asset (a beneficial interest in the trust) and contribution revenue that increases net assets with donor restrictions (see paragraph 958-605-35-3). Museum I would measure its beneficial interest at fair value. That value generally can be measured by the fair value of the assets contributed to the trust.

Example 10: Resource Provider Names Itself As the Specified Beneficiary

If a resource provider transfers assets to a recipient entity and specifies itself or its affiliate as the beneficiary, a presumption that the transfer is reciprocal, and therefore not a contribution, is necessary even if the resource provider explicitly grants the recipient entity variance power. Thus, Symphony Orchestra M would recognize an asset and Community Foundation N would recognize a liability because the transaction is deemed to be reciprocal. Symphony Orchestra M transfers its securities to Community Foundation N in exchange for future distributions. Community Foundation N, by its acceptance of the transfer, agrees that at the time of the transfer, distributions to Symphony Orchestra M are capable of fulfillment and consistent with the foundation’s mission. Although the fair value of those future distributions may not be commensurate with the fair value of the securities given up (because Symphony Orchestra M is at risk of cessation of the distributions), the transaction is accounted for as though those values are commensurate. In comparison, the donors to Community Foundation F in Example 5 (see paragraph 958-605-55-88) explicitly grant variance power to Community Foundation F in a nonreciprocal transfer. In that Example, it is clear that the donors have made a contribution because they retain no beneficial interests in the transferred assets. Because the donors in that Example explicitly grant variance power to Community Foundation F, it, rather than City Botanical Society E, is the recipient of that contribution.

10.10.19.9 ASC 962, Plan Accounting — Defined Contribution Pension Plans

Reporting at Fair Value

Some plan investments may not have Level 1 inputs to measure fair value. Therefore, they will need to be measured in accordance with the other valuation techniques described in Topic 820. Examples include all of the following:

a. Real estate
b. Mortgages or other loans
c. Limited partnerships
d. Restricted securities
e. Unregistered securities
f. Securities that are traded in inactive markets
g. Nontransferable investment contracts.

Both of the following are the obligation of the plan’s trustees, the administrator, and the corporate trustee:

a. To satisfy themselves that all appropriate factors relevant to the value of the investments have been considered
b. To select a method to measure the fair value of the investments.

To the extent considered necessary, the plan may use the services of a specialist to assist the plan (or the administrators) in measuring the fair value of investments. Topic 820 provides guidance on how to measure fair value.
ASC 962-325 (continued)

Implementation Guidance

55-1 The following illustrate fair value and contract value reporting guidance in paragraphs 962-325-35-5 through 35-12 (also see fully benefit-responsive investment contract) for defined-contribution plan investments.

55-2 The value is determined within the context of the objectives of financial statements for a defined contribution plan. The valuation must reflect the ability of the plan to pay benefits from the perspective of the participants. This value is then reflected on participants’ statements to disclose the amount they can expect to receive when they exercise their rights to withdraw, borrow, or transfer funds under the terms of the plan.

A Five-Year Public Bond (or Portfolio of Bonds) Guaranteed by a Third Party to Have a Fixed Value at the End of Three Years

55-3 A five-year public bond (or portfolio of bonds) is guaranteed by a third party to have a fixed value at the end of three years. The guarantee applies only to the extent that the bond (or portfolio) is not liquidated before the end of three years. Liquidation within three years is at fair value.

55-4 Because guaranteed proceeds from the bond are not available for benefit withdrawals or transfers prior to maturity, the contract is not fully benefit-responsive and, therefore, net assets available for benefits shall reflect the fair value for this investment contract. Fair value should be measured in accordance with Topic 820.

A Benefit-Responsive Investment Contract

55-5 A contract provides a fixed crediting interest rate, and a financially responsible entity guarantees liquidity at contract value before maturity for any and all participant-initiated benefit withdrawals, loans, or transfers arising under the terms of the plan, which allows access for all participants on a quarterly basis.

55-6 The net assets available for benefits should reflect the contract value for this investment contract, because the plan will receive such value and only such value if the contract is accessed to pay participant benefits or transfers.

55-7 This contract would be viewed as fully benefit-responsive. Examples of some variations on this contract, and their impact on the valuation, include the following:

a. Liquidity at contract value is not guaranteed for benefits that are attributable to termination of the plan, a plan spinoff to a new employer plan, or amendments to plan provisions. Net assets available for benefits should reflect the contract value for this investment contract, unless it is probable that the plan will be terminated, spun off, or amended.

b. Liquidity at contract value is not guaranteed for benefits that are attributable to the layoff of a large group of workers or an early retirement program. Net assets available for benefits should reflect the contract value for this investment contract, unless it is probable that termination of the employment of a significant number of employees will occur.

c. The contract will pay for benefits of up to 30 percent of the contract at contract value, and any excess benefits will be at some adjusted value. Net assets available for benefits should reflect the fair value for this investment contract because they are not fully benefit-responsive.

d. The contract will pay benefits at contract value, but only if the issuer of the contract determines that there is sufficient liquidity in the portfolio of assets that backs the contract. Because the third party has not guaranteed liquidity for participant-initiated withdrawals, net assets available for benefits should reflect the fair value for this investment contract because they are not fully benefit-responsive.

e. The contract will not pay benefits at contract value if benefits are due to participant transfers to another fixed income investment option, unless the funds are invested in an equity option for at least three months (equity wash provisions). Net assets available for benefits shall reflect the contract value for this investment contract because the contract would be considered fully benefit-responsive.
A Five-Year, Non-Benefit-Responsive Investment Contract That Has No Liquid Market for Trading

55-8 Net assets available for benefits should reflect the fair value for such an investment contract because there is no guarantee of liquidity at contract value. Fair value would be measured in the same manner as for an illiquid bond. Topic 820 includes a discussion of methods used to measure the fair values of illiquid instruments.

A Benefit-Responsive, Participating, Separate Account Investment Contract

55-9 A financially responsible issuer pays contract value for participant withdrawals, regardless of the value of the assets in the separate account. The credited interest rate is a function of the relationship between the contract value and the value of the assets in the separate account. The rate is reset periodically, daily, monthly, quarterly, and so on, by the issuer and cannot be less than zero. There may or may not be a specified maturity date on the contract. The contract holder may terminate the contract at any time, and receive the value of the assets in the separate account.

55-10 Net assets available for benefits should reflect the contract value for this investment contract because participants are guaranteed return of principal and accrued interest.

A Synthetic Investment Contract — Managed Type

55-11 Such a contract operates similarly to a separate account guaranteed investment contract, except that the assets are placed in a trust (with ownership by the plan) rather than a separate account of the issuer and a financially responsible third party issues a wrapper contract that provides that participants can, and must, execute plan transactions at contract value.

55-12 Net assets available for benefits should reflect the contract value for this investment contract because participants are guaranteed return of principal and accrued interest.

A Synthetic Investment Contract — Repurchase Type

55-13 Under such a contract, the plan purchases a bond and places it in trust. The plan then contracts with a financially responsible third party to provide benefit responsiveness. Under the contract, should the bond need to be sold to meet a participant-initiated withdrawal benefit, loan, or transfer, the plan is obligated to sell the bond to the contract issuer, and the issuer is obligated to buy the bond. The transaction price is defined under the contract (for example, amortized cost).

55-14 Net assets available for benefits should reflect the contract value for this investment contract because return of principal and accrued interest has been guaranteed to participants.

55-15 If the contract provided only an option for the sponsor to sell the bond to the issuer, rather than an obligation to do so, reflecting net assets available for benefits at contract value for this investment contract would also apply.

See also Example 2 in ASC 962-325-55-17 for an illustration of the application of ASC 962-325 to the financial statements of a defined contribution plan.
10.10.19.10  ASC 965, Plan Accounting — Health and Welfare Benefit Plans

ASC 965-325

Implementation Guidance

55-1 Implementation guidance in Section 962-325-55 illustrates the guidance in paragraphs 965-325-35-6 through 35-8 for the application of fair value less costs to sell, if significant, and contract value reporting for health and welfare plan investments. In each situation, value is determined within the context of the objectives of financial statements for a defined contribution plan. The valuation must reflect the ability of the plan to pay benefits from the perspective of the participants. This value is then reflected on participants' statements to disclose the amount they can expect to receive when they exercise their rights to withdraw, borrow, or transfer funds under the terms of the plan.

55-2 See paragraph 962-325-55-3 for implementation guidance on a five-year public bond (or portfolio of bonds) that is guaranteed by a third party to have a fixed value at the end of three years.

55-3 See paragraphs 962-325-55-5 through 55-7 for implementation guidance on a fully benefit-responsive investment contract.

55-4 See paragraph 962-325-55-8 for implementation guidance on a five-year, non-benefit-responsive investment contract that has no liquid market for trading.

55-5 See paragraph 962-325-55-10 for implementation guidance on a benefit-responsive participating separate account investment contract.

55-6 See paragraph 962-325-55-12 for implementation guidance on a synthetic contract (managed type).

55-7 See paragraph 962-325-55-13 for implementation guidance on a synthetic investment contract (repurchase type).

Illustrations

55-8 See Example 2 (paragraph 962-325-55-17) for financial statements that illustrate certain applications of the provisions of this Subtopic that apply to the annual financial statements of a defined contribution plan.

10.10.19.11  ASC 970, Real Estate — General

ASC 970-340

Amenities

25-10 Costs of amenities shall be allocated among land parcels benefited and for which development is probable. A land parcel may be considered to be an individual lot or unit, an amenity, or a phase. The fair value of a parcel is affected by its physical characteristics, its highest and best use, and the time and cost required for the buyer to make such use of the property considering access, development plans, zoning restrictions, and market absorption factors.
### 10.10.19.12  **ASC 972, Real Estate — Common Interest Realty Associations**

<table>
<thead>
<tr>
<th>ASC 972-360</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>30-1</strong> Common property recognized as assets of a common interest realty association shall be initially measured at the common interest realty association's cost to acquire it if the common interest realty association acquired the property in a monetary transaction. If the common interest realty association acquired the property in a nonmonetary transaction, such as by a nonreciprocal transfer from the developer, and if the property is recognized as an asset of the common interest realty association, the common interest realty association shall initially measure the property using fair value at the date of its acquisition. It may be helpful to consider the developer's cost, if it is known, in determining the fair value.</td>
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Chapter 11 — Disclosure

11.1 Introduction

11.1.1 Background

The disclosure requirements in ASC 820 apply to items (1) measured at fair value on a recurring or nonrecurring basis and (2) not measured at fair value on a recurring or nonrecurring basis but for which fair value is disclosed in the financial statements. However, they do not apply to fair value measurements at initial recognition. ASC 820’s disclosure requirements related to recurring or nonrecurring fair value measurements after initial recognition apply to all entities other than the plan assets of a defined benefit pension or other postretirement plan in the sponsor’s financial statements. ASC 715 contains fair value disclosure requirements that apply to the plan assets of a defined benefit pension plan or other postretirement plan that is accounted for in accordance with ASC 715.

Under ASC 825, an entity also must provide incremental disclosures about the following:

- The fair value of certain financial instruments, whether recognized or unrecognized in an entity’s statement of financial position.
- Concentrations of credit risk of financial instruments.
- The market risk of financial instruments.
- Eligible items measured at fair value in accordance with the FVO.

This chapter discusses the fair value disclosures required by ASC 820 and the incremental fair value disclosures required by ASC 825 for certain financial instruments. Chapter 12 discusses the incremental disclosures required for eligible items measured at fair value in accordance with the FVO. Appendix A addresses the disclosures required by ASC 715 for plan assets of a defined benefit pension plan or other postretirement plan as well as fair-value-related disclosures required by other Codification topics. The disclosure requirements in ASC 825-10-50-20 through 50-23 related to concentrations of credit risk and market risk of financial instruments are outside the scope of this publication.

Since the issuance of FASB Statement 157, the FASB has amended the fair value disclosure requirements in ASC 715, ASC 820, and ASC 825 on numerous occasions. As of the date of this publication, all entities subject to these requirements will have adopted all of the relevant amendments made in various ASUs, with one exception: some entities will have not adopted, or fully adopted, all of the amendments made by ASU 2018-13 (issued in August 2018), which revised the fair value disclosure requirements in ASC 820. Section 11.1.2 provides more information about the effective date and transition provisions of ASU 2018-13. Sections 11.2 and 11.3 address disclosure requirements in ASC 820 and ASC 825 for entities that have and have not adopted ASU 2018-13, respectively.
11.1.2 ASU 2018-13

11.1.2.1 General

The amendments in ASU 2018-13 are part of a broader FASB project to improve the overall effectiveness of financial statement disclosures. For more information about the ASU’s new, eliminated, and modified disclosure requirements, see Section 11.2 as well as Deloitte’s August 31, 2018, Heads Up.

11.1.2.2 Effective Date and Transition

ASC 820-10


65-12 The following represents the transition and effective date information related to Accounting Standards Update No. 2018-13, Fair Value Measurement (Topic 820): Disclosure Framework — Changes to the Disclosure Requirements for Fair Value Measurement:

a. The pending content that links to this paragraph shall be effective for all entities for fiscal years, and interim periods within those years, beginning after December 15, 2019.

b. An entity shall apply the pending content that links to this paragraph retrospectively to all periods presented, except for the changes in unrealized gains and losses required by paragraph 820-10-50-2(d), the range and weighted-average disclosure required by paragraph 820-10-50-2(bbb)(2)(i), and the narrative description of measurement uncertainty in accordance with paragraph 820-10-50-2(g) that are required to be applied prospectively for only the most recent interim or annual period presented in the initial fiscal year of adoption.

c. Early adoption of the pending content that links to this paragraph is permitted (an entity is permitted to early adopt the removed or modified disclosures in paragraph 820-10-50-2(bb), (c)(3), (f), and (g), paragraph 820-10-50-2G, and paragraph 820-10-50-6A(b) and (e) and adopt the additional disclosures in paragraph 820-10-50-2(bbb)(2)(i) and (d) upon their effective date), including adoption in any interim period for:
   1. Public business entities for periods in which financial statements have not yet been issued
   2. All other entities for periods in which financial statements have not yet been made available for issuance.

ASU 2018-13 is effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early adoption was permitted upon the ASU’s issuance, including in any interim period for which financial statements had not yet been issued or made available for issuance. Further, an entity is permitted to early adopt any removed or modified disclosure requirements while delaying its adoption of other new disclosure requirements until the ASU’s effective date.

Under ASU 2018-13, an entity must apply a retrospective transition approach to all periods presented. However, as detailed in ASC 820-10-65-12(b), certain disclosures are outside the scope of this amendment and are instead provided “prospectively for only the most recent interim or annual period presented in the initial fiscal year of adoption.” These disclosures include:

• Changes in unrealized gains and losses included in OCI (see Section 11.2.3.5.3).

• The range and weighted average used to develop significant unobservable inputs for Level 3 fair value measurements (see Section 11.2.3.5.1.1).

• The narrative description of measurement uncertainty (see Section 11.2.3.5.4).
In paragraph BC74 of ASU 2018-13, the FASB discussed its reasons for prescribing prospective application for these disclosures, stating that “the benefits of retrospective application would not justify the costs for the amendments that would require entities to disclose new quantitative information” and that “qualitatively discussing measurement uncertainty for more than a year in the past seemed outdated."

11.1.3 Applicability of Disclosure Requirements to Certain Entities

ASC 820’s disclosure requirements apply to all entities other than the plan assets of a defined benefit or other postretirement plan that are accounted for in accordance with ASC 715. The disclosure requirements of ASC 820 differ depending on whether an entity is a nonpublic entity. ASC 820-10-20 defines the term “nonpublic entity” as follows:

Any entity that does not meet any of the following conditions:

a. Its debt or equity securities trade in a public market either on a stock exchange (domestic or foreign) or in an over-the-counter market, including securities quoted only locally or regionally.

b. It is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets).

c. It files with a regulatory agency in preparation for the sale of any class of debt or equity securities in a public market.

d. It is required to file or furnish financial statements with the Securities and Exchange Commission.

e. It is controlled by an entity covered by criteria (a) through (d).

In this chapter, any entity that is not a nonpublic entity is referred to as an “other-than-nonpublic entity.”

The ASC 825 fair value disclosure requirements pertaining to financial instruments not recognized at fair value apply only to public business entities. ASC 825-10-20 defines the term “public business entity” as follows:

A public business entity is a business entity meeting any one of the criteria below. Neither a not-for-profit entity nor an employee benefit plan is a business entity.

a. It is required by the U.S. Securities and Exchange Commission (SEC) to file or furnish financial statements, or does file or furnish financial statements (including voluntary filers), with the SEC (including other entities whose financial statements or financial information are required to be or are included in a filing).

b. It is required by the Securities Exchange Act of 1934 (the Act), as amended, or rules or regulations promulgated under the Act, to file or furnish financial statements with a regulatory agency other than the SEC.

c. It is required to file or furnish financial statements with a foreign or domestic regulatory agency in preparation for the sale of or for purposes of issuing securities that are not subject to contractual restrictions on transfer.

d. It has issued, or is a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market.

e. It has one or more securities that are not subject to contractual restrictions on transfer, and it is required by law, contract, or regulation to prepare U.S. GAAP financial statements (including notes) and make them publicly available on a periodic basis (for example, interim or annual periods). An entity must meet both of these conditions to meet this criterion.

An entity may meet the definition of a public business entity solely because its financial statements or financial information is included in another entity’s filing with the SEC. In that case, the entity is only a public business entity for purposes of financial statements that are filed or furnished with the SEC.
11.1.4 Applicability of Disclosure Requirements to Interim Financial Information of Publicly Traded Companies

Publicly traded companies (e.g., SEC registrants) should include the fair value disclosures required by ASC 820 and ASC 825 in their interim financial statements in accordance with ASC 270-10-50-1(k) and 50-1(m). Disclosures related to amounts as of the end of the reporting period (or, for nonrecurring fair value measurements, disclosures related to amounts as of the measurement date) should be provided for the most current date, and any preceding dates, of the statement of financial position that are included in the interim financial statements. The activity-related disclosures (e.g., the Level 3 fair value rollforward information) should be included on a quarterly and year-to-date basis for the current quarter and current year-to-date period, as well as any preceding quarters and year-to-date periods, included in the interim financial statements. Qualitative disclosures should also include information that applies to all the financial reporting periods included in the interim financial statements. The scope of the fair value disclosure requirements for interim financial statements is the same as their scope for annual financial statements (i.e., any exceptions that apply to an entity’s annual financial statements would similarly apply to its interim financial statements).

While the above guidance pertains to publicly traded companies, if interim financial statements are issued by an entity that does not meet the definition of a publicly traded company, those financial statements must also include the disclosures required by ASC 820 and ASC 825 to comply with ASC 270.

11.1.5 Recurring Versus Nonrecurring Fair Value Measurements

An entity must provide the disclosures required by ASC 820 for both recurring and nonrecurring fair value measurements. ASC 820-10-50-2(a) defines recurring and nonrecurring, as used in this context, as follows:

Recurring fair value measurements of assets or liabilities are those that other [Codification topics] require or permit in the statement of financial position at the end of each reporting period. Nonrecurring fair value measurements of assets or liabilities are those that other [Codification topics] require or permit in the statement of financial position in particular circumstances (for example, when a reporting entity measures a long-lived asset or disposal group classified as held for sale at fair value less costs to sell in accordance with [ASC] 360 because the asset’s fair value less costs to sell is lower than its carrying amount).

In other words, assets and liabilities measured at fair value on a recurring basis are those that are remeasured at fair value, after initial recognition, in each financial reporting period. Assets and liabilities measured at fair value on a nonrecurring basis are those that, because of a specific event or circumstance, must be remeasured after initial recognition at fair value in accordance with other
Codification topics. An entity must apply the disclosure requirements in ASC 820 for nonrecurring fair value measurements of assets and liabilities in reporting periods in which (1) those assets or liabilities are subject to fair value remeasurement after initial recognition and (2) the resulting measurement is recognized in the financial statements. In some cases, an item may be remeasured to fair value in consecutive reporting periods but the remeasurement is nonrecurring because the provision in the other Codification topic that requires or permits such measurement does not apply to all changes in fair value (e.g., a long-lived asset or disposal group classified as held for sale may be remeasured to fair value less costs to sell in each financial reporting period until its disposal because there is a decrease in the fair value less costs to sell in each financial reporting period).

For certain assets, other Codification topics require that entities recognize recoveries (not to exceed the original cost basis) of previously recognized impairment losses or lower-of-cost-or-fair-value adjustments (e.g., a recovery of an impairment of a loan classified as held for sale). In such circumstances, the recognized amounts of recoveries that do not exceed the prior write-downs are considered nonrecurring fair value measurements that are subject to ASC 820’s nonrecurring fair value disclosure requirements. However, to the extent that the fair value amount exceeds the original cost basis, the fair value measurement is not subject to these requirements because the amount reflected in the financial statements (i.e., the cost basis) is not a nonrecurring fair value measurement.

The disclosure requirements for nonrecurring fair value measurements are generally less extensive than those for recurring fair value measurements. For example, all entities are exempt from disclosing the following for nonrecurring fair value measurements:

- Transfers between categories of the fair value hierarchy.
- The Level 3 rollforward.
- Unrealized gains and losses for the period that are recognized in income or OCI.
- The narrative description of the uncertainty (or sensitivity) of a Level 3 fair value measurement that results from unobservable inputs.

However, entities must disclose the reason for each nonrecurring fair value measurement and the date or period of the measurement’s recognition, if not as of the date of the statement of financial position. See Sections 11.2.2.1 and 11.3.2.1 for further discussion of the disclosures required for nonrecurring fair value measurements.

Table 11-1 lists examples of recurring and nonrecurring fair value measurements, and Example 11-1 illustrates a nonrecurring fair value measurement of a finite-lived intangible asset. See Section 2.1.2 for further discussion of other Codification topics that permit or require measurement of an item at fair value.
### Table 11-1

<table>
<thead>
<tr>
<th>Examples of Recurring Fair Value Measurements</th>
<th>Examples of Nonrecurring Fair Value Measurements</th>
</tr>
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<tbody>
<tr>
<td>Trading or available-for-sale debt securities within the scope of ASC 320.</td>
<td>Mortgage loans held for sale or mortgage-backed securities held for sale that are remeasured at the lower of cost or fair value in accordance with ASC 948-310-35-1 through 35-3.</td>
</tr>
<tr>
<td>Investments in equity securities that are periodically measured at fair value under ASC 321 (i.e., those with readily determinable fair values or without readily determinable fair values to which the measurement alternative in ASC 321-10-35-2 is not applied).</td>
<td>Investments in equity securities that are accounted for by using the measurement alternative in ASC 321-10-35-2 when (1) an observable price change occurs for the identical or a similar security in accordance with ASC 321-10-35-2 or (2) the security is impaired in accordance with ASC 321-10-35-3.(^1)</td>
</tr>
<tr>
<td>Investments in equity securities with readily determinable fair values or debt securities owned by NFP entities in accordance with ASC 958-320 and ASC 958-321.</td>
<td>Other-than-temporarily impaired equity method investments in accordance with ASC 323-10-35-31 and 35-32.</td>
</tr>
<tr>
<td>Derivative assets and liabilities within the scope of ASC 815, including bifurcated embedded derivatives and hybrid financial instruments that an entity has elected to remeasure at fair value in their entirety.</td>
<td>Impaired loan receivables that, as a practical expedient, are remeasured on the basis of (1) their observable market price in accordance with ASC 310-10-35-22 or (2) the fair value of the collateral if the loan is collateral-dependent in accordance with ASC 310-10-35-22 and ASC 310-10-35-32.</td>
</tr>
<tr>
<td>Investments owned by investment companies in accordance with ASC 946.</td>
<td>Impaired finite-lived intangible assets in accordance with ASC 350-30-35-14.</td>
</tr>
<tr>
<td>Liabilities measured at fair value, with changes in fair value recognized in earnings, in accordance with ASC 480-10-35-5.</td>
<td>Impaired indefinite-lived intangible assets in accordance with ASC 350-30-35-19.</td>
</tr>
<tr>
<td>Nonderivative written call options carried at fair value in accordance with the SEC staff’s long-standing position that written options should be initially and subsequently recognized at fair value.</td>
<td>Impaired goodwill in accordance with ASC 350-20-35-4 through 35-19.</td>
</tr>
<tr>
<td>Financial assets or financial liabilities for which an entity has elected the FVO in accordance with ASC 825 (e.g., certain equity method investments or an entity’s own debt).</td>
<td>Impaired (1) long-lived assets to be held and used, (2) long-lived assets to be disposed of other than by sale, or (3) long-lived assets to be disposed of by sale in accordance with ASC 360-10-35-17 through 35-43.</td>
</tr>
<tr>
<td>Classes of servicing assets or liabilities for which an entity has elected the fair value measurement method in accordance with ASC 860-50-35-1.</td>
<td>Classes of servicing assets or liabilities for which an entity has elected the amortization method in accordance with ASC 860-50-35-1 when those servicing assets are impaired or the fair value of those servicing liabilities has increased above the carrying amount in accordance with ASC 860-50-35-9 through 35-12.</td>
</tr>
</tbody>
</table>

---

\(^1\) ASU 2019-04 clarified that the occurrence of any remeasurement event in ASC 321 for equity securities without readily determinable fair values accounted for under the measurement alternative in accordance with ASC 321-10-35-2 represents a nonrecurring fair value measurement under ASC 820. ASU 2019-04 also added ASC 321-10-50-28, which states:

To the extent that the disclosure requirements in [ASC 321] achieve the fair value disclosure requirements described in [ASC] 820-10-50 on disclosing fair value measurement, an entity need not duplicate the related fair value disclosure.

See ASU 2019-04 for the effective date and transition provisions.
Example 11-1

Nonrecurring Fair Value Measurement of a Finite-Lived Intangible Asset

Company X (which has a calendar year-end) acquires Company Y on December 31, 20X7. In the purchase price allocation, X allocates $100,000 to a finite-lived intangible asset on the basis of its fair value. Assume straight-line amortization of $1,250 per quarter. As of December 31, 20X7, X is not required to include the finite-lived intangible asset in the nonrecurring disclosure table because the only fair value measurement recognized in the financial statements related to the asset occurred at initial recognition.

As of September 30, 20X8, (1) the finite-lived intangible asset is recorded at $96,250 ($3,750 of amortization has occurred since initial recognition); (2) an event or change in circumstances has occurred, indicating that the carrying amount of the asset may not be recoverable (e.g., adverse changes in the business climate); and (3) X has tested the asset for impairment and determined that no impairment exists. The finite-lived intangible asset is not included in the ASC 820 disclosures because no nonrecurring fair value measurement of the asset was recognized in the financial statements during the reporting period.

Because of continued concerns regarding the business climate, X tests the finite-lived intangible asset for impairment as of December 31, 20X8, and records an impairment charge of $5,000 to reduce the carrying amount of the asset to its fair value of $90,000. As of this date, X should include the finite-lived intangible asset in its ASC 820 disclosures because a nonrecurring fair value measurement of the asset was reflected in the statement of financial position during the period.

Because of improvements in the business climate, as of March 31, 20X9, X no longer tests the finite-lived intangible asset for impairment. Company X does not include the asset in the ASC 820 disclosures for the March 31, 20X9, reporting period because a nonrecurring fair value measurement was not recognized in the financial statements during the reporting period.

11.2 Fair Value Disclosures — After Adoption of ASU 2018-13

11.2.1 Objectives and Scope

<table>
<thead>
<tr>
<th>ASC 820-10</th>
</tr>
</thead>
<tbody>
<tr>
<td>50-1C The objective of the disclosure requirements in this Subtopic is to provide users of financial statements with information about assets and liabilities measured at fair value in the statement of financial position or disclosed in the notes to financial statements:</td>
</tr>
<tr>
<td>a. The valuation techniques and inputs that a reporting entity uses to arrive at its measures of fair value, including judgments and assumptions that the entity makes</td>
</tr>
<tr>
<td>b. The uncertainty in the fair value measurements as of the reporting date</td>
</tr>
<tr>
<td>c. How changes in fair value measurements affect an entity's performance and cash flows.</td>
</tr>
</tbody>
</table>

| 50-1D When complying with the disclosure requirements of this Subtopic, a reporting entity shall consider all of the following: |
| a. The level of detail necessary to satisfy the disclosure requirements |
| b. How much emphasis to place on each of the various requirements |
| c. How much aggregation or disaggregation to undertake |
| d. Whether users of financial statements need additional information to evaluate the quantitative information disclosed. |

| 50-2 A reporting entity shall disclose . . . information for each class of assets and liabilities (see paragraph 820-10-50-2B for information on determining appropriate classes of assets and liabilities) measured at fair value (including measurements based on fair value within the scope of this Topic) in the statement of financial position after initial recognition. . . . |
Chapter 11 — Disclosure

ASC 820-10 (continued)

50-2E For each class of assets and liabilities not measured at fair value in the statement of financial position but for which the fair value is disclosed, a reporting entity shall disclose the information required by paragraph 820-10-50-2(b) and (h). . . .

50-10 Plan assets of a defined benefit pension or other postretirement plan that are accounted for in accordance with Topic 715 are not subject to the disclosure requirements in paragraphs 820-10-50-1C through 50-8. Instead, the disclosures required in paragraphs 715-20-50-1(d)(iv) and 715-20-50-5(c)(iv) shall apply for fair value measurements of plan assets of a defined benefit pension or other postretirement plan.

ASC 825-10

50-1 Paragraph 825-10-05-3 identifies various Topics within the Codification that address financial instruments matters. Those and other Topics in the Codification require disclosures about specific financial instruments. This Subsection addresses incremental disclosures about all of the following:

a. Fair value of financial instruments . . . .

Applicability of This Subsection

50-2 This guidance discusses the applicability of the disclosure requirements in this Subsection to entities and transactions.

Entities

50-2A The disclosure guidance in this Subsection applies to public business entities . . . .

Transactions

50-8 In part, this Subsection requires disclosures about fair value for all financial instruments, whether recognized or not recognized in the statement of financial position, except that the disclosures about fair value prescribed in paragraphs 825-10-50-10 through 50-13 and 825-10-50-15 are not required for any of the following:

a. Employers' and plans' obligations for pension benefits, other postretirement benefits including health care and life insurance benefits, postemployment benefits, employee stock option and stock purchase plans, and other forms of deferred compensation arrangements (see Topics 710, 712, 715, 718, and 960)

b. Substantively extinguished debt subject to the disclosure requirements of Subtopic 405-20

c. Insurance contracts, other than financial guarantees (including financial guarantee insurance contracts within the scope of Topic 944) and investment contracts, as discussed in Subtopic 944-20

d. Lease contracts as defined in Topic 840 [Topic 842] (a contingent obligation arising out of a cancelled lease and a guarantee of a third-party lease obligation are not lease contracts and are subject to the disclosure requirements in this Subsection)

e. Warranty obligations (see Topic 450 and the Product Warranties Subsections of Topic 460)

f. Unconditional purchase obligations as defined in paragraph 440-10-50-2

g. Investments accounted for under the equity method in accordance with the requirements of Topic 323

h. Noncontrolling interests and equity investments in consolidated subsidiaries (see Topic 810)

i. Equity instruments issued by the entity and classified in stockholders' equity in the statement of financial position (see Topic 505)

j. Receive-variable, pay-fixed interest rate swaps for which the simplified hedge accounting approach is applied (see Topic 815)

k. Fully benefit-responsive investment contracts held by an employee benefit plan

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ASC 825-10 (continued)

<table>
<thead>
<tr>
<th>ASC 825-10 (continued)</th>
</tr>
</thead>
<tbody>
<tr>
<td>l. Investments in equity securities accounted for under the measurement guidance for equity securities without readily determinable fair values (see Topic 321)</td>
</tr>
<tr>
<td>m. Trade receivables and payables due in one year or less</td>
</tr>
<tr>
<td>n. Deposit liabilities with no defined or contractual maturities</td>
</tr>
<tr>
<td>o. Liabilities resulting from the sale of prepaid stored-value products within the scope of paragraph 405-20-40-3.</td>
</tr>
</tbody>
</table>

50-9 Generally accepted accounting principles (GAAP) require disclosure of or subsequent measurement at fair value for many classes of financial instruments. Those requirements are not superseded or modified by this Subsection.

ASC 820 and ASC 825 require entities to disclose fair value information about the following assets and liabilities:

- Those that are measured at fair value in the statement of financial position in a financial reporting period after initial recognition (except for the plan assets of a defined benefit pension or other postretirement plan that is subject to the fair value disclosure requirements in ASC 715).
- Those that are not measured at fair value in the statement of financial position but for which the fair value is disclosed.

All assets and liabilities that are measured at fair value on a recurring or nonrecurring basis are subject to the disclosure requirements in ASC 820. An entity is not required to provide fair value disclosures for assets, liabilities, and instruments classified in a reporting entity's shareholders' equity that are initially recognized at fair value in accordance with ASC 820. However, other Codification topics may require specific fair value disclosures. See Chapter 2 for more information about the scope of ASC 820, including the application of the ASC 820 disclosure requirements to specific types of assets and liabilities. See Appendix A for a discussion of other Codification topics that require incremental fair value disclosures, including disclosures about fair value on initial recognition.

ASC 825 specifies the fair value disclosure requirements that apply to certain financial instruments, regardless of whether they are recognized in the statement of financial position. These disclosures, which only public business entities are required to provide, include disclosures about financial instruments that are not measured at fair value on a recurring or nonrecurring basis (e.g., financial assets and financial liabilities measured at amortized cost). ASC 825-10-50-8 provides exceptions from the disclosure requirements for certain financial instruments. See Chapter 2 for more information about the scope of ASC 825, including the application of its disclosure requirements to specific types of financial assets and financial liabilities.

ASC 820-10-50-1C and 50-1D outline the objective of the fair value disclosure requirements in ASC 820, along with matters for entities to consider in complying with these requirements. An entity may need to use significant judgment in determining the information to disclose and the level of detail (and aggregation or disaggregation) at which to provide such disclosures. In using such judgment, entities should consider the needs of present and potential investors, creditors, donors, and other financial statement users. Entities may determine that it is necessary to provide supplemental information (i.e., disclosures in addition to those required by ASC 820) in certain circumstances. See Section 11.2.3.1 for more information about determining classes of assets and liabilities for disclosure purposes.
Chapter 11 — Disclosure

Connecting the Dots

ASC 820-10-15-1 indicates that in the absence of a specific exception, “[ASC 820] applies when another [Codification topic] requires or permits fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements).” Thus, entities have the option of providing ASC 820 and ASC 825 disclosures for assets or liabilities for which such disclosures are not required. An entity may wish to disclose fair value information for certain assets and liabilities to give a more complete picture of their value or to provide supplemental information that is considered helpful to users of the entity’s financial statements.

There are various matters to consider regarding the voluntary disclosure of fair value information for assets and liabilities for which the disclosures in ASC 820 or ASC 825 are not required. Such considerations include the following:

- In addition to disclosing a fair value amount, an entity should consider the incremental disclosure requirements in ASC 820-10-50-2E for assets and liabilities not measured at fair value in the statement of financial position but for which the fair value is disclosed (see ASC 820-10-50-2(b) and ASC 820-10-50-2(h)). For such assets and liabilities, ASC 820-10-50-2E would not require the disclosure of other fair value information, such as the valuation technique, the inputs used in the valuation technique, and the quantitative disclosures about significant unobservable inputs for fair value amounts classified in Level 3 of the fair value hierarchy. However, entities can voluntarily include such disclosures for any asset or liability that is not measured at fair value in the statement of financial position.

- An entity should apply a rational and consistent policy when disclosing such fair value information (e.g., from one reporting period and asset or liability to another). The entity should also ensure that its disclosures clearly indicate that such assets and liabilities for which fair value is voluntarily disclosed are not recognized at fair value on a recurring or nonrecurring basis in the statement of financial position and should separately identify the associated carrying amounts reported in the statement of financial position. This is especially important when an entity has assets or liabilities of a similar type and some but not all of those assets or liabilities are recognized at fair value in the statement of financial position.

See Section 2.3.2.2.4 for discussion of voluntary fair value disclosures of equity method investments.

The remaining discussion in this section focuses on the disclosure requirements in ASC 820 and ASC 825 (for financial assets and financial liabilities of public business entities). Also see ASC 820-10-55-99 through 55-107 for examples illustrating disclosures that are not reproduced in the discussion below.
11.2.2 Disclosure Requirements

11.2.2.1 Assets and Liabilities Measured at Fair Value in the Statement of Financial Position

**ASC 820-10**

50-2 A reporting entity shall disclose the following information for each class of assets and liabilities (see paragraph 820-10-50-2B for information on determining appropriate classes of assets and liabilities) measured at fair value (including measurements based on fair value within the scope of this Topic) in the statement of financial position after initial recognition:

a. For recurring fair value measurements, the fair value measurement at the end of the reporting period, and for nonrecurring fair value measurements, the fair value measurement at the relevant measurement date and the reasons for the measurement. Recurring fair value measurements of assets or liabilities are those that other Topics require or permit in the statement of financial position at the end of each reporting period. Nonrecurring fair value measurements of assets or liabilities are those that other Topics require or permit in the statement of financial position in particular circumstances (for example, when a reporting entity measures a long-lived asset or disposal group classified as held for sale at fair value less costs to sell in accordance with Topic 360 because the asset's fair value less costs to sell is lower than its carrying amount). For nonrecurring measurements estimated at a date during the reporting period other than the end of the reporting period, a reporting entity shall clearly indicate that the fair value information presented is not as of the period's end as well as the date or period that the measurement was taken.

b. For recurring and nonrecurring fair value measurements, the level of the fair value hierarchy within which the fair value measurements are categorized in their entirety (Level 1, 2, or 3). . .

bbb. The information shall include:

1. For recurring and nonrecurring fair value measurements categorized within Level 2 and Level 3 of the fair value hierarchy, a description of the valuation technique(s) and the inputs used in the fair value measurement. If there has been a change in either or both a valuation approach and a valuation technique (for example, changing from matrix pricing to the binomial model or the use of an additional valuation technique), the reporting entity shall disclose that change and the reason(s) for making it.

2. For recurring and nonrecurring fair value measurements categorized within Level 3 of the fair value hierarchy, a reporting entity shall provide quantitative information about the significant unobservable inputs used in the fair value measurement. A reporting entity is not required to create quantitative information to comply with this disclosure requirement if quantitative unobservable inputs are not developed by the reporting entity when measuring fair value (for example, when a reporting entity uses prices from prior transactions or third-party pricing information without adjustment). However, when providing this disclosure, a reporting entity cannot ignore quantitative unobservable inputs that are significant to the fair value measurement and are reasonably available to the reporting entity. Employee benefit plans, other than those plans that are subject to the U.S. Securities and Exchange Commission's (SEC) filing requirements, are not required to provide this disclosure for investments held by an employee benefit plan in their plan sponsor's own nonpublic equity securities, including equity securities of their plan sponsor's nonpublic affiliated entities.

i. In complying with (bbb)(2), a reporting entity shall provide the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements. A reporting entity shall disclose how it calculated the weighted average (for example, weighted by relative fair value). For certain unobservable inputs, a reporting entity may disclose other quantitative information, such as the median or arithmetic average, in lieu of the weighted average, if such information would be a more reasonable and rational method to reflect the distribution of unobservable inputs used to develop the Level 3 fair value measurement. An entity does not need to disclose its reason for omitting the weighted average in these cases.

ii. A nonpublic entity is not required to provide the information described in (bbb)(2)(i), but is required to provide quantitative information about the significant unobservable inputs used in the fair value measurement in accordance with (bbb)(2).
c. For recurring fair value measurements categorized within Level 3 of the fair value hierarchy, a reconciliation from the opening balances to the closing balances, disclosing separately changes during the period attributable to the following:
   1. Total gains or losses for the period recognized in earnings (or changes in net assets), and the line item(s) in the statement of income (or activities) in which those gains or losses are recognized
   1a. Total gains or losses for the period recognized in other comprehensive income, and the line item(s) in other comprehensive income in which those gains or losses are recognized
   2. Purchases, sales, issues, and settlements (each of those types of changes disclosed separately)
   3. The amounts of any transfers into or out of Level 3 of the fair value hierarchy and the reasons for those transfers. Transfers into Level 3 shall be disclosed and discussed separately from transfers out of Level 3. See paragraph 820-10-50-2C for additional guidance.

d. For recurring fair value measurements categorized within Level 3 of the fair value hierarchy, the amount of the total gains or losses for the period in (c)(1) included in earnings (or changes in net assets) and in (c)(1a) included in other comprehensive income that is attributable to the change in unrealized gains or losses relating to those assets and liabilities held at the end of the reporting period, and the line item(s) in the statement(s) of comprehensive income (or activities) in which those unrealized gains or losses are recognized.

g. For recurring fair value measurements categorized within Level 3 of the fair value hierarchy, a narrative description of the uncertainty of the fair value measurement from the use of significant unobservable inputs if those inputs reasonably could have been different at the reporting date. For example, how a change in those significant unobservable inputs to a different amount might result in a significantly higher or lower fair value measurement at the reporting date. If there are interrelationships between those inputs and other unobservable inputs used in the fair value measurement, a reporting entity shall also provide a description of those interrelationships and of how they might magnify or mitigate the effect of changes in the unobservable inputs on the fair value measurement. To comply with that disclosure requirement, the narrative description of the uncertainty of the fair value measurement that would result from using unobservable inputs shall include the unobservable inputs disclosed when complying with paragraph 820-10-50-2(bbb).

h. For recurring and nonrecurring fair value measurements, if the highest and best use of a nonfinancial asset differs from its current use, a reporting entity shall disclose that fact and why the nonfinancial asset is being used in a manner that differs from its highest and best use.

50-2B A class of assets and liabilities will often require greater disaggregation than the line items presented in the statement of financial position. However, a reporting entity shall provide information sufficient to permit reconciliation to the line items presented in the statement of financial position.

50-2D If a reporting entity makes an accounting policy decision to use the exception in paragraph 820-10-35-18D, it shall disclose that fact.

50-2F A nonpublic entity is not required to disclose the information required by paragraph 820-10-50-2(bbb)(2X)i), (d), and (g) and paragraph 820-10-50-2E unless required by another Topic.

50-2G In lieu of paragraph 820-10-50-2(c), a nonpublic entity shall disclose separately changes during the period attributable to the following:
   a. Purchases and issues (each of those types of changes disclosed separately)
   b. The amounts of any transfers into or out of Level 3 of the fair value hierarchy and the reasons for those transfers. Transfers into Level 3 shall be disclosed and discussed separately from transfers out of Level 3. See paragraph 820-10-50-2C for additional guidance.
ASC 820-10 (continued)

50-3 For derivative assets and liabilities, the reporting entity shall present both of the following:
   a. The fair value disclosures required by paragraph 820-10-50-2(a) through (b) on a gross basis (which is consistent with the requirement of paragraph 815-10-50-4B(a))
   b. The reconciliation disclosure required by paragraph 820-10-50-2(c) through (d) on either a gross or a net basis.

50-4A For a liability measured at fair value and issued with an inseparable third-party credit enhancement, an issuer shall disclose the existence of that credit enhancement.

50-7 As discussed in paragraph 250-10-50-5, the disclosures required by Topic 250 for a change in accounting estimate are not required for revisions resulting from a change in a valuation technique or its application.

50-8 A reporting entity shall present the quantitative disclosures required by this Topic in a tabular format.

All assets and liabilities measured in the statement of financial position at fair value after initial recognition are subject to the disclosure requirements in ASC 820-10-50-2. The nature and extent of such disclosures differ depending on the following:

- Whether the reporting entity is a nonpublic entity (see Section 11.1.3).
- Whether the fair value measurement is recurring or nonrecurring (see Section 11.1.5).

Table 11-2 below summarizes the disclosures an entity is required to provide under ASC 820 when, in accordance with other Codification topics, an asset or liability is measured at fair value in the statement of financial position after initial recognition. This table distinguishes between (1) other-than-nonpublic and nonpublic entities and (2) recurring and nonrecurring fair value measurements. As noted in ASC 820-10-50-8, the quantitative disclosures must be presented in a tabular format. See the remaining subsections of Section 11.2 for more information about these required disclosures.

Table 11-2

<table>
<thead>
<tr>
<th>Required Disclosures and Applicable References&lt;sup&gt;a&lt;/sup&gt;</th>
<th>Entities Other Than Nonpublic Entities</th>
<th>Nonpublic Entities</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Recurring</td>
<td>Nonrecurring</td>
</tr>
<tr>
<td>Fair value as of the reporting date or relevant measurement date (ASC 820-10-50-2(a) and ASC 825-10-50-10)</td>
<td>X</td>
<td>X&lt;sup&gt;b&lt;/sup&gt;</td>
</tr>
<tr>
<td>The reason for the fair value measurement (ASC 820-10-50-2(a))</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>The level in the fair value hierarchy (ASC 820-10-50-2(b) and ASC 825-10-50-10)</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>For fair value measurements in Levels 2 and 3 of the fair value hierarchy, a description of the valuation techniques and inputs used in the fair value measurement (ASC 820-10-50-2(bbb)(1))</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>For fair value measurements in Levels 2 and 3 of the fair value hierarchy, if there has been a change in a valuation approach, a valuation technique, or both, the nature of, and reason for, that change (ASC 820-10-50-2(bbb)(1))</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Required Disclosures and Applicable References&lt;sup&gt;(a)&lt;/sup&gt;</td>
<td>Entities Other Than Nonpublic Entities</td>
<td>Nonpublic Entities</td>
</tr>
<tr>
<td>-------------------------------------------------</td>
<td>-------------------------------------</td>
<td>-----------------</td>
</tr>
<tr>
<td>If the highest and best use of a nonfinancial asset differs from its current use, disclosure of that fact and why the asset is being used in such a way (ASC 820-10-50-2(h))</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Information sufficient to permit reconciliation of (1) disclosures about classes of assets and liabilities by level in the fair value hierarchy and (2) line items presented in the statement of financial position (ASC 820-10-50-2B)</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>If an entity makes an accounting policy decision to use the net risk position valuation exception in ASC 820-10-35-18D, disclosure of that fact (ASC 820-10-50-2D)</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>For liabilities measured at fair value, the existence of any credit enhancement and whether it is reflected in the fair value measurement (ASC 820-10-50-4A)</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td><strong>The disclosures below apply only to Level 3 fair value measurements.</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Quantitative information about the significant unobservable inputs used in the fair value measurement (ASC 820-10-50-2(bbb)(2))</td>
<td>X&lt;sup&gt;(c)&lt;/sup&gt;</td>
<td>X&lt;sup&gt;(c),(d)&lt;/sup&gt;</td>
</tr>
<tr>
<td>In complying with the requirement in ASC 820-10-50-2(bbb)(2) to disclose quantitative information about significant unobservable inputs, an entity would disclose the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements and how the weighted average was calculated. For certain unobservable inputs, an entity may disclose other quantitative information, such as the median or arithmetic average, in lieu of the weighted average, if using such information would be a more reasonable and rational method for reflecting the distribution of unobservable inputs used to develop the fair value measurement (ASC 820-10-50-2(bbb)(2)(i))</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>The Level 3 fair value rollforward (ASC 820-10-50-2(c))</td>
<td>X</td>
<td>(g)</td>
</tr>
<tr>
<td>Total amount of gains and losses for the period, recorded in current income and OCI, that is attributable to the change in unrealized gains and losses for assets or liabilities held at the end of the reporting period and the line items in which such amounts are recognized (ASC 820-10-50-2(d))</td>
<td>X</td>
<td>(f)</td>
</tr>
</tbody>
</table>
(Table continued)

<table>
<thead>
<tr>
<th>Required Disclosures and Applicable References&lt;sup&gt;(a)&lt;/sup&gt;</th>
<th>Entities Other Than Nonpublic Entities</th>
<th>Nonpublic Entities</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Recurring</td>
<td>Nonrecurring</td>
</tr>
<tr>
<td>Narrative description of the uncertainty of the fair value measurement with respect to the use of significant unobservable inputs (i.e., those disclosed in ASC 820-10-50-2(bbb)), if those inputs could reasonably have been different on the reporting date, and a description of the interrelationships between unobservable inputs, including how such interrelationships might magnify or mitigate the impact of changes in such inputs on fair value (ASC 820-10-50-2(g))</td>
<td>X</td>
<td></td>
</tr>
</tbody>
</table>

Notes to table:

<sup>(a)</sup> Entities that have early adopted ASU 2018-13 may delay their adoption of the ASU's new disclosure requirements. These requirements apply only to other-than-nonpublic entities and include (1) changes in unrealized gains or losses included in OCI for recurring Level 3 fair value measurements held at the end of the reporting period and (2) disclosure of the range and weighted average used to develop significant unobservable inputs for Level 3 fair value measurements.

<sup>(b)</sup> ASC 820-10-50-2(a) requires disclosure of a nonrecurring fair value measurement amount as of the date of the measurement (e.g., the impairment or recovery date), which may differ from the end of the reporting period. ASC 820-10-50-2(a) states, in part, that “[f]or nonrecurring measurements estimated at a date during the reporting period other than the end of the reporting period, a reporting entity shall clearly indicate that the fair value information presented is not as of the period’s end as well as the date or period that the measurement was taken.” ASC 820-10-50-2B further states, in part, that “a reporting entity shall provide information sufficient to permit reconciliation to the line items presented in the statement of financial position.” These disclosure requirements address situations for which the amounts disclosed under ASC 820 for assets or liabilities measured at fair value on a nonrecurring basis during the period are not consistent with the amounts recorded in the statement of financial position for such assets or liabilities. See also Section 11.2.3.3.2.

<sup>(c)</sup> ASC 820-10-50-2(bbb)(2) states, in part:

A reporting entity is not required to create quantitative information to comply with this disclosure requirement if quantitative unobservable inputs are not developed by the reporting entity when measuring fair value (for example, when a reporting entity uses prices from prior transactions or third-party pricing information without adjustment). However, when providing this disclosure, a reporting entity cannot ignore quantitative unobservable inputs that are significant to the fair value measurement and are reasonably available to the reporting entity. Employee benefit plans, other than those plans that are subject to the U.S. Securities and Exchange Commission’s (SEC) filing requirements, are not required to provide this disclosure for investments held by an employee benefit plan in their plan sponsor’s own nonpublic equity securities, including equity securities of their plan sponsor’s nonpublic affiliated entities.

<sup>(d)</sup> This disclosure is not required for fair value measurements related to the financial accounting and reporting for goodwill after its initial recognition (see ASC 350-20-50-3).

<sup>(e)</sup> For nonpublic entities, this disclosure is not required for fair value measurements related to the financial accounting and reporting for (1) goodwill after its initial recognition (see ASC 350-20-50-3) and (2) indefinite-lived intangible assets after their initial recognition (ASC 350-30-50-3A).

<sup>(f)</sup> ASC 820-10-50-2F exempts nonpublic entities from providing this disclosure unless it is required by another Codification topic.

<sup>(g)</sup> In lieu of providing this disclosure, in accordance with ASC 820-10-50-2G, a nonpublic entity should separately disclose changes during the period that are attributable to (1) purchases and issues (each of these types of changes should be disclosed separately) and (2) the amounts of any transfers into or out of Level 3 of the fair value hierarchy and the reasons for those transfers (transfers into Level 3 should be disclosed separately from transfers out of Level 3).

See ASC 820-10-50-3 for additional disclosure requirements related to derivative assets and liabilities.
Changing Lanes

To make it easier for entities to exercise discretion when complying with the fair value disclosure requirements, the FASB removed “at a minimum” from the phrase “a reporting entity shall disclose, at a minimum” in ASC 820-10-50-2 (amended by ASU 2018-13). The purpose of this amendment was to clarify that it is appropriate for entities and their auditors to consider materiality when evaluating the fair value measurement disclosure requirements.

SEC Considerations

Section 9700 of the FRM states:

In March and September 2008, the Division of Corporation Finance sent illustrative letters to certain public companies that reported significant amounts of asset-backed securities, loans carried at fair value or the lower of cost or market, and derivative assets and liabilities in their recent 10-K filings. The letters highlight disclosure matters relating to SFAS 157 [ASC 820], and suggest disclosures that companies may consider in preparing their MD&A.

These letters highlight disclosure matters that SEC registrants should consider in complying with SEC Regulation S-K, Item 303, which addresses the preparation of MD&A. While certain of the recommended disclosures are now required under U.S. GAAP as a result of amendments to ASC 820, SEC registrants should consider the disclosures suggested in these letters that are not otherwise provided in the notes to the financial statements.

11.2.2.2 Assets and Liabilities Not Measured at Fair Value in the Statement of Financial Position

<table>
<thead>
<tr>
<th>ASC 820-10</th>
</tr>
</thead>
<tbody>
<tr>
<td>50-2E For each class of assets and liabilities not measured at fair value in the statement of financial position but for which the fair value is disclosed, a reporting entity shall disclose the information required by paragraph 820-10-50-2(b) and (h). However, a reporting entity is not required to provide the quantitative disclosures about significant unobservable inputs used in fair value measurements categorized within Level 3 of the fair value hierarchy required by paragraph 820-10-50-2(bbb)(2). For such assets and liabilities, a reporting entity does not need to provide the other disclosures required by this Topic.</td>
</tr>
<tr>
<td>50-2F A nonpublic entity is not required to disclose the information required by paragraph 820-10-50-2(bbb)(2)), (d), and (g) and paragraph 820-10-50-2E unless required by another Topic.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>ASC 825-10</th>
</tr>
</thead>
<tbody>
<tr>
<td>50-2A The disclosure guidance in this Subsection applies to public business entities . . . .</td>
</tr>
<tr>
<td>50-9 Generally accepted accounting principles (GAAP) require disclosure of or subsequent measurement at fair value for many classes of financial instruments. Those requirements are not superseded or modified by this Subsection.</td>
</tr>
<tr>
<td>50-10 A reporting entity shall disclose either in the body of the financial statements or in the accompanying notes, the fair value of financial instruments and the level of the fair value hierarchy within which the fair value measurements are categorized in their entirety (Level 1, 2, or 3).</td>
</tr>
</tbody>
</table>

For financial instruments recognized at fair value in the statement of financial position, the disclosure requirements of Topic 820 also apply.
**ASC 825-10 (continued)**

50-11 Fair value disclosed in the notes shall be presented together with the related carrying amount in a form that clarifies both of the following:

a. Whether the fair value and carrying amount represent assets or liabilities
b. How the carrying amounts relate to what is reported in the statement of financial position.

50-12 If the fair value of financial instruments is disclosed in more than a single note, one of the notes shall include a summary table. The summary table shall contain the fair value and related carrying amounts and cross-references to the location(s) of the remaining disclosures required by this Section.

50-13 This Subtopic does not prohibit an entity from disclosing separately the estimated fair value of any of its nonfinancial intangible and tangible assets and nonfinancial liabilities.

50-15 In disclosing the fair value of a financial instrument, an entity shall not net that fair value with the fair value of other financial instruments — even if those financial instruments are of the same class or are otherwise considered to be related (for example, by a risk management strategy) — except to the extent that the offsetting of carrying amounts in the statement of financial position is permitted under either of the following:

a. The general principle in paragraph 210-20-45-1
b. The exceptions for master netting arrangements in paragraph 815-10-45-5 and for amounts related to certain repurchase and reverse repurchase agreements in paragraphs 210-20-45-11 through 45-17.

Public business entities must provide additional fair value disclosures for certain financial assets and financial liabilities that are not measured at fair value in the statement of financial position, which may include financial assets or financial liabilities that were subject to a nonrecurring fair value measurement during a financial reporting period. This disclosure requirement is included in ASC 825-10-50-10 and is also addressed in ASC 820-10-50-2E. In accordance with that guidance, public business entities must disclose the following for financial assets and financial liabilities that are not (1) recognized at fair value in the statement of financial position and (2) subject to an exception in ASC 825-10-50-8:

- The fair value as of the reporting date (i.e., the date of the statement of financial position).
- The level of the fair value hierarchy (Level 1, 2, or 3) within which each fair value measurement is categorized in its entirety.

These disclosures can be included in the body of the financial statements or in the notes and may be provided by classes of assets and liabilities (see Section 11.2.3.1), subject to the prohibitions against netting described in ASC 825-10-50-15. ASC 825-10-50-11 and 50-12 address considerations related to including such disclosures in the notes to the financial statements.

The fair value disclosures should be consistent with the unit of account. For example, as discussed in ASC 825-10-25-13, “[f]or the issuer of a liability issued with an inseparable third-party credit enhancement . . ., the unit of accounting for the liability . . . disclosed at fair value does not include the third-party credit enhancement.”

While an entity is not precluded from also disclosing information about the valuation technique and inputs used, changes in the valuation approach or valuation technique, and significant unobservable inputs, these disclosures are not required for financial assets and financial liabilities that are not measured at fair value in the statement of financial position. ASU 2018-09 clarified that the disclosure

---

2 ASC 820-10-50-2E also refers to the disclosure requirement in ASC 820-10-50-2(h). However, since public business entities are not required to disclose the fair value of nonfinancial assets that are not recognized at fair value, it is unlikely that this disclosure will be relevant to the disclosure of the fair values of items not recognized at fair value.
addressed in ASC 820-10-50-2(bbb) is not required for financial assets and financial liabilities that are not measured at fair value.

Entities other than public business entities are not required to provide disclosures about the fair value of financial assets and financial liabilities that are not measured at fair value in the statement of financial position. Further, ASU 2019-04 clarified that such entities do not need to disclose the fair values of held-to-maturity classified debt securities.

See Section 11.4 for examples of financial instruments that are subject to the disclosure requirements of ASC 825-10-50-10.

### 11.2.2.3 Certain Entities That Calculate NAV per Share (or Its Equivalent)

ASC 820-10

| Fair Value Measurements of Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent) |
| --- | --- |
| 50-6A For investments that are within the scope of paragraphs 820-10-15-4 through 15-5 and that are measured using the practical expedient in paragraph 820-10-35-59 on a recurring or nonrecurring basis during the period, a reporting entity shall disclose information that helps users of its financial statements to understand the nature and risks of the investments and whether the investments, if sold, are probable of being sold at amounts different from net asset value per share (or its equivalent, such as member units or an ownership interest in partners' capital to which a proportionate share of net assets is attributed). A reporting entity shall disclose the following information for each class of investment: |
| a. The fair value measurement (as determined by applying paragraphs 820-10-35-59 through 35-62) of the investments in the class at the reporting date and a description of the significant investment strategies of the investee(s) in the class. |
| b. For each class of investment that includes investments that can never be redeemed with the investees, but the reporting entity receives distributions through the liquidation of the underlying assets of the investees, the period of time over which the underlying assets are expected to be liquidated by the investees if the investee has communicated the timing to the reporting entity or announced the timing publicly. If the timing is unknown, the reporting entity shall disclose that fact. |
| c. The amount of the reporting entity's unfunded commitments related to investments in the class. |
| d. A general description of the terms and conditions upon which the investor may redeem investments in the class (for example, quarterly redemption with 60 days' notice). |
| e. The circumstances in which an otherwise redeemable investment in the class (or a portion thereof) might not be redeemable (for example, investments subject to a lockup or gate). Also, for those otherwise redeemable investments that are restricted from redemption as of the reporting entity's measurement date, the reporting entity shall disclose when the restriction from redemption might lapse if the investee has communicated that timing to the reporting entity or announced the timing publicly. If the timing is unknown, the reporting entity shall disclose that fact and how long the restriction has been in effect. |
| f. Any other significant restriction on the ability to sell investments in the class at the measurement date. . . . |
| g. If a group of investments would otherwise meet the criteria in paragraph 820-10-35-62 but the individual investments to be sold have not been identified (for example, if a reporting entity decides to sell 20 percent of its investments in private equity funds but the individual investments to be sold have not been identified), the investments continue to qualify for the practical expedient in paragraph 820-10-35-59, the reporting entity shall disclose its plans to sell and any remaining actions required to complete the sale(s). |

ASC 820-10-35-59 permits entities, as a practical expedient, to estimate the fair value of an investment within the scope of ASC 820-10-15-4 and 15-5 by using the NAV per share (or its equivalent, such as member units or an ownership interest in partners' capital to which a proportionate share of net assets is attributed) of the investment, provided that it is calculated in a manner consistent with the
measurement principles of ASC 946 as of the reporting entity’s measurement date. To help financial statement users understand the nature and risks of the investments and whether it is probable that they will be sold (if they are sold) at amounts that differ from the NAV per share (or its equivalent), ASC 820-10-50-6A requires specific disclosures, for each interim and annual period, for investment classes within the scope of ASC 820-10-15-4 and 15-5 that an entity measured during the period on a recurring or nonrecurring basis by using the practical expedient in ASC 820-10-35-59. See ASC 820-10-55-107 for an example illustrating such disclosures.

Although investments that an entity records when using the practical expedient in ASC 820-10-35-59 are not categorized within the fair value hierarchy, ASC 820-10-35-54B still requires such an entity to provide the amounts that it measured by using the practical expedient so that the fair value of investments included in the fair value hierarchy can be reconciled to the line items presented in the statement of financial position in accordance with ASC 820-10-50-2B.

Entities are not required to apply the practical expedient in ASC 820-10-35-59 to all investments within the scope of ASC 820-10-15-4 and 15-5. When the practical expedient is not used for such investments, the disclosures outlined in ASC 820-10-50-6A are not required. Rather, as stated in paragraph BC11 of ASU 2015-07, “the fair value of the investment will be included in the fair value hierarchy on the basis of the relative observability of the inputs used in the valuation and subject to the disclosure requirements of [ASC] 820-10-50-2.”

Changing Lanes
Under the guidance in ASU 2018-13, entities are no longer required to estimate and disclose the timing of liquidity events for investments measured at NAV per share (or its equivalent). Instead, the requirement to disclose such events applies only when they have been communicated to reporting entities by investees or announced publicly. If the timing is unknown, entities must disclose that fact. The objective of this change is to prevent an investor from having to make its own estimate when it does not have knowledge of the timing from the investee or another public source.

11.2.3 Interpretive Guidance
11.2.3.1 Identifying Classes of Assets and Liabilities
11.2.3.1.1 General

<table>
<thead>
<tr>
<th>ASC 820-10</th>
</tr>
</thead>
<tbody>
<tr>
<td>50-2B A reporting entity shall determine appropriate classes of assets and liabilities on the basis of the following:</td>
</tr>
<tr>
<td>a. The nature, characteristics, and risks of the asset or liability</td>
</tr>
<tr>
<td>b. The level of the fair value hierarchy within which the fair value measurement is categorized.</td>
</tr>
</tbody>
</table>

The number of classes may need to be greater for fair value measurements categorized within Level 3 of the fair value hierarchy because those measurements have a greater degree of uncertainty and subjectivity. Determining appropriate classes of assets and liabilities for which disclosures about fair value measurements should be provided requires judgment. A class of assets and liabilities will often require greater disaggregation than the line items presented in the statement of financial position. However, a reporting entity shall provide information sufficient to permit reconciliation to the line items presented in the statement of financial position. If another Topic specifies the class for an asset or a liability, a reporting entity may use that class in providing the disclosures required in this Topic if that class meets the requirements in this paragraph.

See Sections 2.2.2 and 10.9 for further discussion of this practical expedient.
In complying with the fair value disclosure requirements of ASC 820-10-50-2, an entity must determine appropriate classes of assets and liabilities in accordance with ASC 820-10-50-2B. An entity must use judgment and carefully consider the facts and circumstances in disaggregating assets and liabilities into separate classes. Such disaggregation often results in a more granular presentation for fair value disclosure purposes than the line items in the statement of financial position. Under ASC 820-10-50-2B, the classes of assets and liabilities should generally be consistent throughout all the fair value disclosures provided in accordance with ASC 820-10-50-2(a)-(h). Therefore, the classes of assets and liabilities used to prepare the quantitative disclosures required by ASC 820-10-50-2(bbb)(2) should generally not differ from the classes included in the other disclosures required by ASC 820-10-50-2.

When determining the appropriate level of disaggregation into classes of assets and liabilities, entities should consider the nature, characteristics, and risk profile of the assets and liabilities, as well as the level of the fair value hierarchy within which each fair value measurement has been categorized. Entities may also consider guidance in other Codification topics (e.g., ASC 320, ASC 815) when making this determination. ASC 320-10-50-1B provides guidance on class determination and useful considerations related to assessing the nature of and risks associated with debt securities. On the basis of those requirements, concentrations are likely to be important in the determination of class for all assets and liabilities.

When preparing quantitative disclosures about significant unobservable inputs used in Level 3 fair value measurements, an entity may discover that:

- Different techniques are used for individual assets, liabilities, or subclasses within a previously identified class of asset or liability.
- Different inputs are being used even when the same technique is used to measure different assets, liabilities, or subclasses within a class.
- The quantitative information varies significantly between one asset, liability, or subclass and others within a class.

Such differences may indicate that the nature, characteristics, or risks of assets, liabilities, or subclasses within a previously identified class differ and that it would be appropriate to create more classes. When disaggregating an asset or liability class because techniques, inputs, or quantitative information about inputs differs, an entity should consider disaggregating the class in other disclosures required by ASC 820-10-50-2(a)-(h) to ensure consistency.

An entity that does not use the same classes throughout its fair value disclosures should consider reconciling, for example, the classes of assets and liabilities categorized in Level 3 of the fair value hierarchy between the leveling disclosures (see ASC 820-10-50-2(b)) and the quantitative disclosures about significant unobservable inputs (see ASC 820-10-50-2(bbb)(2)). Entities should also keep in mind the requirement from ASC 820-10-50-2B to “provide information sufficient to permit reconciliation to the line items presented in the statement of financial position.”
The following examples illustrate disaggregation of assets into classes by using various approaches:

**Example 11-2**

**Aggregation by Valuation Technique**

Entity A holds residential mortgage-backed securities (RMBSs) backed by both prime (i.e., higher credit quality) and subprime (i.e., lower credit quality) mortgages. When identifying the class of asset for disclosure purposes, A concludes that the nature, risks, and characteristics (including valuation technique) of these assets are sufficiently similar to allow aggregation of all RMBSs into one class. Entity A prepares the disclosure below. However, if A holds material amounts of RMBSs backed by mortgages of significantly differing credit quality, this disclosure may not provide sufficient information for financial statement users to understand and evaluate the quantitative information provided. In such a case, A could consider an alternative such as the one presented in Example 11-3 below.

<table>
<thead>
<tr>
<th>Asset</th>
<th>Fair Value (000s)</th>
<th>Valuation Technique(s)</th>
<th>Unobservable Input(s)</th>
<th>Low</th>
<th>High</th>
<th>Weighted Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>RMBS</td>
<td>$9,000</td>
<td>Discounted cash flow</td>
<td>Constant prepayment rate</td>
<td>0.00%</td>
<td>10.00%</td>
<td>2.01%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Loss severity</td>
<td>50.00%</td>
<td>100.00%</td>
<td>60.56%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Constant default rate</td>
<td>0.00%</td>
<td>29.00%</td>
<td>11.78%</td>
</tr>
</tbody>
</table>

**Example 11-3**

**Disaggregation by Risk**

This presentation alternative results in more relevant information for financial statement users than the approach in Example 11-2 above, enabling them to better understand and evaluate the techniques and inputs used. In particular, disaggregating the asset class gives users insight into the different assumptions used when risk and other characteristics differ. Because the guidance that applies to determination of class for this disclosure is the same as the guidance that applies to determination of class for a disclosure of fair value by level in the fair value hierarchy (i.e., the requirement in ASC 820-10-50-2(b)), it would be a best practice to use the same classes for both. When an entity does not use the same classes (e.g., in providing disclosures about fair value by level in the fair value hierarchy and quantitative disclosures about significant unobservable inputs), the entity should provide a reconciliation so that the relationship between the classes is clear.

<table>
<thead>
<tr>
<th>Asset</th>
<th>Fair Value (000s)</th>
<th>Valuation Technique(s)</th>
<th>Unobservable Input(s)</th>
<th>Low</th>
<th>High</th>
<th>Weighted Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>RMBS — prime</td>
<td>$7,000</td>
<td>Discounted cash flow</td>
<td>Constant prepayment rate</td>
<td>0.00%</td>
<td>8.30%</td>
<td>2.30%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Loss severity</td>
<td>50.00%</td>
<td>70.00%</td>
<td>55.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Constant default rate</td>
<td>0.00%</td>
<td>18.00%</td>
<td>10.00%</td>
</tr>
<tr>
<td>RMBS — subprime</td>
<td>$2,000</td>
<td>Discounted cash flow</td>
<td>Constant prepayment rate</td>
<td>0.00%</td>
<td>10.00%</td>
<td>1.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Loss severity</td>
<td>60.00%</td>
<td>100.00%</td>
<td>80.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Constant default rate</td>
<td>0.00%</td>
<td>29.00%</td>
<td>18.00%</td>
</tr>
</tbody>
</table>
Chapter 11 — Disclosure

11.2.3.1.2 Derivative Contracts

ASC 815-10-50 requires entities to provide tabular disclosures about derivatives by “type of contract.” Depending on the facts and circumstances, the classes of derivative contracts under the ASC 820 fair value disclosure requirements may differ from the type of contracts used to provide tabular disclosures under ASC 815. The classes of derivative contracts may be more disaggregated under ASC 820 than the type of contract under ASC 815 but generally should not be more condensed.

An entity should consider the types of derivative contracts it holds. Under ASC 820-10-50-2B, class is based on the derivatives’ characteristics, nature, risks, and classification in the fair value hierarchy. Class is often at a greater level of disaggregation than the line items in the statement of financial position. Therefore, in determining the characteristics, nature, and risks of its derivative contracts, an entity should consider the following factors (in addition to the type of contracts):

- The valuation techniques and inputs used to determine fair value.
- The classification in the fair value hierarchy.
- The level of disaggregation in the statement of financial position.

An entity may also consider the level of disaggregation it uses for other ASC 815 disclosures (e.g., qualitative and volume), which may vary from the level of disaggregation it uses for the ASC 815 tabular disclosures.

ASC 320-10-50-1B provides guidance on class determination and useful considerations related to assessing nature and risks for debt securities. On the basis of those requirements, concentrations are likely to be important in the determination of class for all assets and liabilities. For example, an entity that engages in material commodity transactions may consider concentrations by commodity type, or an entity with a material foreign exchange portfolio may consider concentrations by discrete currencies.

11.2.3.1.3 Disposal Group or Assets to Be Disposed Of

An entity may have a long-lived asset disposal group classified as held for sale under ASC 360 (which may include or represent a discontinued operation). The individual assets and liabilities within a disposal group that are measured at fair value on a recurring or nonrecurring basis are subject to the disclosure requirements in ASC 820.

When considering the appropriate classes of assets and liabilities under ASC 820-10-50-2B and preparing fair value disclosures, an entity should distinguish assets and liabilities that are part of a disposal group classified as held for sale from its other assets and liabilities. This separate presentation is consistent with the requirements in ASC 205-20-45-10 and 45-11 and ASC 360-10-45-14, under which an entity must separately disclose the major classes of assets and liabilities of the discontinued operation (or the major classes of assets and liabilities classified as held for sale) either on the face of the statement of financial position or in the notes to the financial statements. The ASC 820 disclosures required for certain items within a disposal group should be consistent with the disclosures under ASC 205-20-45-10 and 45-11 or ASC 360-10-45-14.

---

4 The assets and liabilities of an asset group to be held and used in an entity’s business would also be subject to ASC 820’s disclosure requirements if they are measured at fair value on a recurring or nonrecurring basis.
ASC 360-10-35-43 requires an entity to measure a disposal group at the lower of its carrying amount or fair value less costs to sell. Furthermore, ASC 360-10-35-40 states:

A loss shall be recognized for any initial or subsequent write-down to fair value less cost to sell. A gain shall be recognized for any subsequent increase in fair value less cost to sell, but not in excess of the cumulative loss previously recognized (for a write-down to fair value less cost to sell). The loss or gain shall adjust only the carrying amount of a long-lived asset, whether classified as held for sale individually or as part of a disposal group.

ASC 820-10-50-2(a) requires an entity to disclose, “[f]or recurring fair value measurements, the fair value measurement at the end of the reporting period, and for nonrecurring fair value measurements, the fair value measurement at the relevant measurement date and the reasons for the measurement.” ASC 820-10-55-100 includes an example of a nonrecurring disclosure.

In certain circumstances, an impairment loss may be recognized for some assets within a disposal group that also includes assets and liabilities measured at fair value on a recurring basis. Thus, the asset group contains assets that are measured on both a recurring and nonrecurring basis. In periods in which an impairment of a disposal group is recognized, the nonrecurring fair value disclosures related to that impairment should reflect the incremental amount beyond what has already been disclosed in the recurring and nonrecurring fair value tables for the other assets and liabilities that are included in the disposal group. See Example 11-4 below.

**Example 11-4**

**Disposal Group for Which There Are Recurring and Nonrecurring Fair Value Measurements**

In November 20X9, Entity B, a calendar-year-end company, enters into an agreement to sell Subsidiary X. The transaction is expected to close in May 201X. In accordance with ASC 360-10-45-9, X is a disposal group that B presents as held for sale in its December 31, 20X9, balance sheet.

Assume the following:

- The disposal group consists of PP&E and equity securities (real estate industry) measured at fair value through earnings. Subsidiary X does not have intangible assets, goodwill, or liabilities.
- The PP&E has a carrying value of $30 million.
- The fair value of the equity securities (real estate industry) is $65 million, measured on the basis of a quoted price in an active market (Level 1).
- The fair value of the disposal group is $80 million, measured on the basis of significant unobservable inputs (Level 3).
- The cost of selling the disposal group is $10 million.

Therefore, on B’s balance sheet, the disposal group is shown as consisting of $70 million of assets held for sale ($80 million fair value less $10 million costs to sell). The disclosures required by ASC 820-10-50-2(a) and 50-2(b) could be presented in the manner described below.

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5 The same approach would apply to long-lived assets held and used that constitute an asset group.
Example 11-4 (continued)

For the assets measured at fair value on a recurring basis during the period, B would present the following:

<table>
<thead>
<tr>
<th>($ in millions)</th>
<th>Fair Value Measurements Using</th>
</tr>
</thead>
<tbody>
<tr>
<td>Description</td>
<td>Year Ended 12/31/X9</td>
</tr>
<tr>
<td>Assets Held for Sale</td>
<td></td>
</tr>
<tr>
<td>Equity securities</td>
<td></td>
</tr>
<tr>
<td>Equity securities — real estate industry</td>
<td>$65</td>
</tr>
<tr>
<td>Total</td>
<td>$65</td>
</tr>
</tbody>
</table>

For the assets measured at fair value on a nonrecurring basis during the period, in addition to narrative disclosures about why this remeasurement was made, B would present the following:

<table>
<thead>
<tr>
<th>($ in millions)</th>
<th>Fair Value Measurements Using</th>
</tr>
</thead>
<tbody>
<tr>
<td>Description</td>
<td>Year Ended 12/31/X9</td>
</tr>
<tr>
<td>Disposal group*</td>
<td>$15</td>
</tr>
<tr>
<td>Total</td>
<td>$15</td>
</tr>
</tbody>
</table>

* The total fair value measurement of the disposal group is $80 million, which includes $65 million of equity securities (real estate industry) included in the disclosure regarding assets and liabilities that are measured at fair value on a recurring basis. The remaining fair value for the disposal group is $15 million.

In calculating the fair value amounts for the above disclosure, X considers the guidance in ASC 360 on impairment or disposal of long-lived assets. Subsidiary X (i.e., the disposal group) has a carrying amount of $95 million (PP&E of $30 million and equity securities (real estate industry) of $65 million) and a fair value of $80 million (which includes $65 million of equity securities in real estate). When considering the costs to sell of $10 million, X recognizes an impairment loss of $25 million in earnings for the period (i.e., $80 million fair value, less $95 million carrying cost, less selling costs of $10 million). This loss is recorded as a write-down of the carrying amount of the long-lived assets within the disposal group.

Note that the above presentations represent one alternative; entities should determine that the disclosure objectives in ASC 205-20, ASC 360, and ASC 820, as appropriate, are met for an asset group or disposal group. The entity would also be subject to (1) the disclosure requirements in both ASC 205-20-50 and ASC 360-10-50 and (2) other relevant fair value disclosure requirements in ASC 820-10-50-2.
11.2.3.2 Disclosures Related to the Fair Value Hierarchy

11.2.3.2.1 General

ASC 820-10-50-2(b) requires all entities to disclose the level of the fair value hierarchy within which all recurring and nonrecurring fair value measurements are categorized. ASC 820-10-50-2E and ASC 825-10-50-10 also require public business entities to disclose the level of the fair value hierarchy for assets and liabilities that are not measured at fair value but for which fair value is disclosed. Such classifications in the fair value hierarchy are made on the basis of the classification of the asset or liability in its entirety.

Fair value measurements often consist of multiple inputs that span multiple levels within the fair value hierarchy. In these circumstances, the asset or liability is classified in its entirety on the basis of the lowest-level input that is deemed significant to the fair value measurement. See Section 8.1.2 for more information.

11.2.3.2.2 Transfers Between Levels

<table>
<thead>
<tr>
<th>ASC 820-10-50-2C</th>
</tr>
</thead>
<tbody>
<tr>
<td>50-2C A reporting entity shall consistently follow its policy for determining when transfers between levels of the fair value hierarchy are deemed to have occurred. The policy about the timing of recognizing transfers shall be the same for transfers into the levels as for transfers out of the levels. Examples of policies for determining the timing of transfers include the following:</td>
</tr>
<tr>
<td>a. The date of the event or change in circumstances that caused the transfer</td>
</tr>
<tr>
<td>b. The beginning of the reporting period</td>
</tr>
<tr>
<td>c. The end of the reporting period.</td>
</tr>
</tbody>
</table>

ASC 820-10-50-2C requires all entities to develop and consistently apply a “policy for determining when transfers between levels of the fair value hierarchy are deemed to have occurred.” However, ASC 820 does not prescribe a method for determining the timing of transfers between levels. Rather, ASC 820-10-50-2C indicates that to determine when transfers have occurred, entities may use the fair value of the asset, liability, or instrument classified in a reporting entity’s shareholders’ equity as of (1) the “date of the event or change in circumstances that caused the transfer,” (2) the “beginning of the reporting period,” or (3) the “end of the reporting period,” provided that the approach applied is used consistently. Accordingly, it is not appropriate for an entity to determine the amount of “transfers in” by using the beginning-of-period fair value and the amount of “transfers out” by using the end-of-period fair value, or vice versa. Such an approach is not acceptable because no gain or loss would be attributed to items transferred into or out of Level 3, thus diminishing the usefulness of the Level 3 rollforward disclosure.

After adopting ASU 2018-13, entities are no longer required to disclose either of the following:

- Transfers between Levels 1 and 2 of the fair value hierarchy for assets and liabilities held at the end of the reporting period that are measured at fair value on a recurring basis (other-than-nonpublic entities were previously required to provide this disclosure).
- Their accounting policy for determining when transfers are deemed to have occurred.

---

6 Assets measured on a recurring basis by using the NAV practical expedient are not subject to such disclosure requirements. See Section 11.2.2.3 for more information.

7 ASC 820-10-50-2(bb) previously required other-than-nonpublic entities to disclose “the amounts of any transfers between Level 1 and Level 2 of the fair value hierarchy, the reasons for those transfers, and the reporting entity’s policy for determining when transfers between levels are deemed to have occurred”; transfers into each level were “disclosed and discussed separately from transfers out of each level.” However, nonpublic entities did not need to provide this disclosure unless they were required to do so by another Codification topic.
Thus, in accordance with ASC 820-10-50-2(c)(3) and ASC 820-10-50-2G(b), all entities that have adopted ASU 2018-13 are only required to disclose the “amounts of any transfers into or out of Level 3 of the fair value hierarchy and the reasons for those transfers.” Further, transfers into Level 3 would be “disclosed and discussed separately from transfers out of Level 3.” While entities are not required to disclose their accounting policy for determining when transfers between levels are recognized, they may determine that such disclosure is useful and provide it anyway.

**Connecting the Dots**

An entity commonly measures the fair value of its assets and liabilities more frequently (e.g., monthly) for internal management reporting purposes than for external reporting purposes. As part of its periodic fair value measurement processes, the entity may incorporate a system for identifying the date of the transfers into or out of Level 3. The fair value amount for transfers determined through the entity’s periodic (i.e., monthly) process could then be used to furnish the disclosures required by ASC 820-10-50-2(c)(3) and ASC 820-10-50-2G(b) at the end of the reporting period.

Example 11-5 illustrates how an entity may determine the date of transfers into or out of Level 3.

### Example 11-5

**Transfers Into or Out of Level 3 of the Fair Value Hierarchy**

Assume the following:
- Entity C holds two securities and is preparing its quarterly financial statements for the period ended September 30, 20X0.
- Security A, which is classified in Level 2 at the beginning of the period (July 1, 20X0), is transferred into Level 3 on July 15, 20X0.
- Security B, which is classified in Level 3 at the beginning of the period (July 1, 20X0), is transferred out of Level 3 (into Level 2) on August 15, 20X0.

The following table illustrates the fair values under the three acceptable methods for disclosing the relevant transfers into and out of Level 3 in accordance with ASC 820-10-50-2C:

<table>
<thead>
<tr>
<th>Security</th>
<th>Method 1 Actual Date of Transfer Fair Value*</th>
<th>Method 2 Beginning of the Reporting Period Fair Value (July 1, 20X0)</th>
<th>Method 3 End of the Reporting Period Fair Value (September 30, 20X0)</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>125 (July 15, 20X0)</td>
<td>150</td>
<td>50</td>
</tr>
<tr>
<td>B</td>
<td>250 (August 15, 20X0)</td>
<td>150</td>
<td>300</td>
</tr>
</tbody>
</table>

* Identifies the date on which transfers in and/or out are deemed to occur on the basis of specific events.
Example 11-5 (continued)

**Analysis**

<table>
<thead>
<tr>
<th>Impact on Levels</th>
<th>Method 1 Actual Date of Transfer Fair Value</th>
<th>Method 2 Beginning of the Reporting Period Fair Value</th>
<th>Method 3 End of the Reporting Period Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Security A</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Level 2 transfer-out value</td>
<td>(125)</td>
<td>(150)</td>
<td>(50)</td>
</tr>
<tr>
<td>Level 3 transfer-in value</td>
<td>125</td>
<td>150</td>
<td>50</td>
</tr>
<tr>
<td>Gain (loss) reflected in Level 3 rollforward</td>
<td>(75)</td>
<td>(100)</td>
<td>—</td>
</tr>
<tr>
<td>Security B</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Level 2 transfer-in value</td>
<td>250</td>
<td>150</td>
<td>300</td>
</tr>
<tr>
<td>Level 3 transfer-out value</td>
<td>(250)</td>
<td>(150)</td>
<td>(300)</td>
</tr>
<tr>
<td>Gain (loss) reflected in Level 3 rollforward</td>
<td>100</td>
<td>—</td>
<td>150</td>
</tr>
</tbody>
</table>

11.2.3.2.3 Cash Collateral Receivables and Payables

See Section 11.2.3.5.2.3.5 for discussion of the presentation of cash collateral receivables and payables related to derivative instruments.

11.2.3.2.4 Assets and Liabilities of a CFE

Under ASC 810, an entity that consolidates an eligible CFE may elect to measure the less observable of the fair value of the CFE’s financial assets or the fair value of the CFE’s financial liabilities by using the more observable of the two measurements. See Section A.19 for information about the additional disclosures an entity is required to provide when it makes this election. See Section 8.1.2 for discussion of the determination of the level of the fair value hierarchy in which an entity should categorize the less observable fair value measurement.

11.2.3.3 Reconciliation of Disclosures to the Statement of Financial Position

11.2.3.3.1 General

Under ASC 820, entities must reconcile the disclosed fair value amounts to the statement of financial position when:

- The classes of assets or liabilities are more disaggregated than the line items in the statement of financial position (see Section 11.2.3.1).
- The amount of an asset or liability on the date of the statement of financial position does not equal the amount of a nonrecurring fair value measurement that was recognized for the asset or liability during the financial reporting period (see Section 11.2.3.3.2).
- An entity estimates the fair value of certain investments by using NAV per share as a practical expedient (see Section 11.2.3.3.3).
11.2.3.3.2 Nonrecurring Fair Value Measurements

ASC 820-10-50-2(a) requires entities to disclose, for nonrecurring fair value measurements, the fair value as of the measurement date and the reasons for the measurement. ASC 820-10-50-2(b) further requires disclosure of the level of the nonrecurring fair value measurement within the fair value hierarchy, which is also determined as of the measurement date. If a nonrecurring fair value measurement occurs on any date other than the date of an entity’s statement of financial position, the entity must, as stated in ASC 820-10-50-2(a), “clearly indicate that the fair value information presented is not as of the period’s end as well as the date or period that the measurement was taken.” In meeting this objective, entities should consider the guidance in ASC 820-10-50-2B, which states, in part, that “a reporting entity shall provide information sufficient to permit reconciliation to the line items presented in the statement of financial position.” Thus, the entity should provide supplemental information that reconciles (1) the ASC 820 nonrecurring fair value amounts disclosed and (2) the carrying amount as of the date of the statement of financial position.

For example, assume that a long-lived asset classified as held and used is impaired from its current carrying value of $100 to its fair value of $75 as of November 30, 20X7 (assume a calendar-year-end entity). In this case, the amount disclosed as a nonrecurring fair value measurement will be $75. However, since the asset is held and used, subsequent amortization through December 31, 20X7 (the balance sheet date), is recognized. Assume that $1 of subsequent amortization is recognized in December 20X7. The balance sheet will reflect the amortization, while the nonrecurring disclosure will not. The entity should provide supplemental information that reconciles the ASC 820 nonrecurring amount disclosed to the recorded amount as of the balance sheet date.

In addition, the amount of a nonrecurring fair value measurement may not equal the recognized amount of the asset or liability subject to such measurement on the date the measurement is recognized. For example, ASC 360-10-35-43 requires that a disposal group classified as held for sale be measured at the lower of its carrying amount or fair value less costs to sell. However, ASC 820 clarifies that costs to sell (transaction costs) are not included in a fair value measurement. Thus, when an impairment of a long-lived asset classified as held for sale has occurred during a financial reporting period, the nonrecurring fair value amount disclosed under ASC 820 will not be consistent with the carrying amount reflected in the balance sheet as of the reporting date. As previously stated, entities should provide supplemental information that reconciles the ASC 820 nonrecurring disclosure amount to the recorded amount as of the balance sheet date. See notes (c)–(e) of Example 9 in ASC 820-10-55-100 for an illustration of such disclosure.

11.2.3.3.3 Certain Entities That Calculate NAV per Share (or Its Equivalent)

As discussed in Section 11.2.2.3, although investments that an entity records when using the practical expedient in ASC 820-10-35-59 are not categorized within the fair value hierarchy, an entity is still required under ASC 820-10-35-54B to provide the amounts that it measured by using the practical expedient so that the fair value of investments included in the fair value hierarchy can be reconciled to the line items presented in the statement of financial position in accordance with ASC 820-10-50-2B. ASC 820-10-50-6A further requires that entities “disclose [additional] information that helps users of [their] financial statements to understand the nature and risks of the investments.” See Note (f) of Example 9 in ASC 820-10-55-100 for an illustration of such disclosure.

11.2.3.4 Disclosure of Valuation Techniques and Inputs

ASC 820-10-50-2(bbb)(1) requires entities to disclose (1) a description of the valuation technique(s) and inputs for each class of assets and liabilities measured at fair value on a recurring or nonrecurring basis and classified within Level 2 or Level 3 of the fair value hierarchy and (2) any changes in a valuation
approach, valuation technique, or both in connection with such measurements, as well as the reasons for such changes. In accordance with ASC 820-10-50-7, a change in the valuation approach or valuation technique does not cause an entity to be subject to the disclosure requirements in ASC 250 related to a change in accounting estimate.

The objective of these disclosure requirements is to help financial statement users understand not only the valuation techniques and inputs but also the judgments the entity uses when measuring fair value. To meet this objective, entities should consider disclosing the following information about the valuation techniques and inputs used in Level 2 and Level 3 fair value measurements:

- Whether the entity can choose between various valuation techniques and how it makes that choice.
- A description of the valuation techniques selected and the risks or shortcomings (if any) of those techniques.
- When a model is used, a description of the model and related inputs, as well as how the inputs are sourced.
- If the valuation technique has changed since previous reporting periods, the reason why the entity made the change and a quantification of the change's impact on the financial statements.
- The methods the entity uses to calibrate models to market prices and how frequently it uses these methods.
- A description of the use of broker quotes or pricing services. Such a description may include:
  - How many quotes were obtained, how these quotes were verified, and which brokers or pricing services the entity used and why.
  - A summary of known valuation techniques used by brokers and pricing services and to what extent observable market information, as opposed to unobservable market information, was used to determine the quote.
  - Whether quotes are adjusted and how the ultimate fair value was determined.
  - Whether a quote is binding or nonbinding.
- When an entity measures fair value by using prices for similar instruments, how the entity adjusts these prices to reflect the characteristics of the instruments subject to the measurement.
- The key drivers of value for each significant Level 2 and Level 3 asset/liability class and the extent to which the inputs used are observable or unobservable.
- An entity's consideration of illiquidity when performing the valuation. Factors to consider include:
  - Specific assumptions used.
  - How the assumptions were developed.
  - How and why assumptions changed from period to period.
  - Whether valuation techniques/models changed as a result of the lack of liquidity.
  - Whether alternative valuation techniques for illiquid instruments would have resulted in materially different fair values.
- How the entity's and counterparty's nonperformance risk was taken into consideration in the valuation (e.g., for derivatives or debt instruments).
ASC 820-10-55-103 and 55-104 provide examples illustrating how an entity might comply with the requirement to disclose the valuation techniques and inputs used in the measurement of fair value.

For Level 3 fair value measurements, entities are also required to disclose quantitative information about the significant unobservable inputs used in the measurement (see ASC 820-10-50-2(bbb)(2)), and for recurring fair value measurements, other-than-nonpublic entities must provide a narrative description of the uncertainty of the fair value measurement with respect to the use of significant unobservable inputs (see ASC 820-10-50-2(g)). Entities are permitted, but not required, to disclose quantitative information about inputs used in Level 1 or Level 2 fair value measurements (i.e., the information that must be disclosed about Level 2 fair value measurements in ASC 820-10-50-2(bbb)(1) may be qualitative instead of quantitative). See Sections 11.2.3.5.1 and 11.2.3.5.4 for more information about the disclosures of unobservable inputs related to Level 3 fair value measurements.

11.2.3.5 Level 3 Measurements

11.2.3.5.1 Quantitative Information About Significant Unobservable Inputs

ASC 820-10-50-2(bbb)(2) requires entities to disclose, for each class of assets and liabilities measured at fair value on a recurring or nonrecurring basis in the statement of financial position after initial recognition, “quantitative information about the significant unobservable inputs used” in those Level 3 fair value measurements. In complying with this requirement, other-than-nonpublic entities must, in accordance with ASC 820-10-50-2(bbb)(2)(i), “provide the range and weighted average of significant unobservable inputs used to develop” those Level 3 fair value measurements. ASC 820-10-50-2(bbb)(2)(ii) clarifies that nonpublic entities are exempt from disclosing this information but are still required to provide quantitative information about significant unobservable inputs used in Level 3 fair value measurements. All entities are exempt from disclosing quantitative information about inputs used in Level 1 and Level 2 fair value measurements; however, entities are permitted to provide disclosures for those measurements when they are similar to the quantitative disclosures of significant inputs required for Level 3 fair value measurements.

In a manner consistent with the FASB's stated objectives in requiring the aforementioned disclosures, entities must determine the following in providing the Level 3 disclosures required for significant unobservable inputs:

- The types of quantitative information to disclose (see Section 11.2.3.5.1.1).
- How detailed the disclosures should be (i.e., the level of aggregation or disaggregation) (see Section 11.2.3.5.1.2).
- What information should be provided, if any, when the entity uses prices from prior transactions or third-party pricing information (see Section 11.2.3.5.1.3).

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8 See footnotes (d) and (e) of Table 11-2 for exceptions to this disclosure requirement.
9 Paragraph BC86 of ASU 2011-04 states, in part: The Boards noted that the objective of the disclosure is not to enable users of financial statements to replicate the reporting entity's pricing models but to provide enough information for users to assess whether the reporting entity's views about individual inputs differed from their own and, if so, to decide how to incorporate the reporting entity's fair value measurement in their decisions. The Boards concluded that the information required by the disclosure will facilitate comparison of the inputs used over time, providing users with information about changes in management's views about particular unobservable inputs and about changes in the market for the assets and liabilities within a particular class. In addition, that disclosure might facilitate comparison between reporting entities with similar assets and liabilities categorized within Level 3 of the fair value hierarchy.
Changing Lanes
Before ASU 2018-13 was issued, entities were required to disclose a description of the valuation processes used for all recurring and nonrecurring Level 3 fair value measurements. The FASB concluded that the benefits of this disclosure requirement did not outweigh its costs to users of the financial statements; ASU 2018-13 therefore superseded ASC 820-10-50-2(f) and the related implementation guidance in ASC 820-10-55-105.

11.2.3.5.1.1 Types of Quantitative Information
Entities must use judgment in deciding what types of quantitative information to provide about significant unobservable inputs. In complying with the guidance in ASC 820-10-50-2(bbb)(2)(i), other-than-nonpublic entities are required to disclose the following:

- The range and weighted average used to develop these inputs.
- How that weighted average was calculated for each fair value measurement categorized within Level 3 of the fair value hierarchy.

However, entities may disclose other quantitative information, such as median or arithmetic average, in lieu of the weighted average if they determine that providing such disclosures constitutes a more reasonable and rational method of reflecting the distribution of significant unobservable inputs used to develop Level 3 fair value measurements. Paragraph BC51 of ASU 2018-13 cites the use of unobservable inputs to develop fair value measurements of derivative instruments as an example of when it would be more reasonable and rational to use other quantitative information, rather than a weighted average, to reflect the distribution of significant unobservable inputs used to develop Level 3 fair value measurements. In this and similar cases, entities are not required to disclose their reasons for omitting the weighted average. See ASC 820-10-55-103 for an example illustrating this disclosure requirement.

In determining which disclosures to provide, an entity should consider whether the information it plans to furnish would enable a reasonable investor (or another financial statement user, such as a regulator) to assess the entity's views on individual inputs. An entity may determine that it needs to provide information in addition to that required in ASC 820-10-50-2(bbb)(2) to appropriately convey the nature and significance of inputs used. Such information may include narrative disclosures, other types of quantitative information (e.g., mean, median, standard deviation), and other alternatives.

In addition, ASC 820-10-55-104 states that “a reporting entity should provide additional information that will help users of its financial statements to evaluate the quantitative information disclosed.” For example, ASC 820-10-55-104(a) lists the following information that an entity might consider disclosing for RMBSs:

1. The types of underlying loans (for example, prime loans or subprime loans)
2. Collateral
3. Guarantees or other credit enhancements
4. Seniority level of the tranches of securities
5. The year of issue
6. The weighted-average coupon rate of the underlying loans and the securities
7. The weighted-average maturity of the underlying loans and the securities
8. The geographical concentration of the underlying loans
9. Information about the credit ratings of the securities.
Further, ASC 820-10-55-104(b) indicates that for all assets and liabilities, entities should consider disclosing "[h]ow third-party information such as broker quotes, pricing services, net asset values, and relevant market data was taken into account when measuring fair value." In doing so, entities should consider clearly identifying the fair value of assets and liabilities measured by using third-party information.

### 11.2.3.5.1.2 Disaggregation of Inputs

Entities must disclose quantitative information about all significant unobservable inputs. The meaning of the term “significant” in this context is the same as that in ASC 820-10-35-37A, which states, in part:

> [A] fair value measurement is categorized in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement. Assessing the significance of a particular input to the entire measurement requires judgment, taking into account factors specific to the asset or liability.

ASC 820 does not establish a bright line for significance or mandate that significance be determined quantitatively or be based on any specific quantitative approach. ASC 820-10-35-37A notes that an entity must use judgment in determining significance, “taking into account factors specific to the asset or liability.” Entities should establish a method for determining whether an input is significant to a fair value measurement in its entirety and should apply it consistently. As discussed in Section 8.1.2, one possible method for determining whether an input is significant to a fair value measurement is to use a threshold or percentage of the overall measurement amount as a benchmark for significance. In determining significance when using a particularly complex valuation technique, an entity may need to consider how a particular input or inputs behave within a reasonable range of expected outcomes (i.e., by performing a sensitivity analysis).

While the process described in Section 8.1.2 is generally used to identify only the lowest-level input that is significant to the measurement in its entirety, the same process can be used to identify all significant unobservable inputs. The following is a summary of the process described in Section 8.1.2, modified to highlight considerations uniquely relevant to ASC 820-10-50-2(bbb)(2):

1. Determine a threshold or percentage of the overall measurement amount as a benchmark for significance. An entity may determine the threshold by considering whether a reasonable investor would believe that variations in underlying inputs and the resultant variations in fair value measurements would significantly alter the total mix of information available. In making this determination, entities may consider SEC SAB Topic 1.M and PCAOB Auditing Standard 11. “Significance” is not the same as “materiality,” but entities can apply similar concepts to this determination.

2. Inventory all inputs used in a Level 3 fair value measurement (i.e., make a list and ensure that it is complete).

3. Perform a sensitivity analysis for each unobservable input by recalculating fair value, altering the unobservable input so that fair value is calculated by using the low and high values in a range of reasonably possible alternative values for that input. In identifying a range of reasonably possible alternative values, entities could consider (1) prevailing market conditions, (2) input from internal or external specialists, or (3) known or implied amounts in sales or transfer transactions observed for similar assets or liabilities.

4. Determine whether the percentage change in fair value resulting from the sensitivity analysis in step 3 exceeds the benchmark for significance identified in step 1.

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10 As noted in Section 8.1.2, an entity should not use a percentage of a particular component of a fair value measurement or the income statement effect of a fair value measurement (i.e., the threshold should be based on a balance sheet approach).
5. Because SEC and PCAOB guidance on materiality clearly notes that materiality is not solely a quantitative concept, supplement the quantitative analysis in step 4 with a consideration of qualitative factors such as the nature of the input (e.g., for certain derivatives, all inputs may be considered significant).

6. If the input is determined to be significant on the basis of the above steps, include the input in the tabular fair value disclosure.

7. Repeat these steps for other unobservable inputs identified in step 2.

8. Aggregate individually insignificant inputs by level to determine whether a combination of such inputs is significant to the measurement in its entirety. If so, disclose these inputs.

This process would not need to be repeated in each reporting period unless facts and circumstances change. In identifying significant inputs, management may also consider (1) specialists' input; (2) competitors' disclosures, analyst reports, or both; and (3) its own judgment based on experience with the products.

11.2.3.5.1.3 Third-Party Pricing Information

Paragraph BC90 of ASU 2011-04 states the following regarding quantitative disclosures about significant unobservable inputs related to use of third-party pricing information:

The Boards understand that fair value is sometimes measured on the basis of prices in prior transactions (for example, adjustments to the last round of financing for a venture capital investment) or third-party pricing information (for example, broker quotes). Such measurements might be categorized within Level 3 of the fair value hierarchy. In such cases, the Boards concluded that the reporting entity should be required to disclose how it has measured the fair value of the asset or liability, but that it should not need to create quantitative information (for example, an implied market multiple or future cash flows) to comply with the disclosure requirement if quantitative information other than the prior transaction price or third-party pricing information is not used when measuring fair value. However, the Boards concluded that when using a prior transaction price or third-party pricing information a reporting entity cannot ignore other quantitative information that is reasonably available. If there was an adjustment to the price in a prior transaction or third-party pricing information that is significant to the fair value measurement in its entirety, that adjustment would be an unobservable input about which the reporting entity would disclose quantitative information, even if the reporting entity does not disclose the unobservable information used when pricing the prior transaction or developing the third-party pricing information.

In considering the guidance in paragraph BC90 of ASU 2011-04, an entity must disclose the following information about its Level 3 fair value measurements:

- How it has used third-party pricing information to measure the fair value of assets or liabilities.
- Quantitative information about significant unobservable inputs used to develop significant adjustments, if any, that the entity applies to third-party pricing information (or prior transactions).
- Quantitative information about significant unobservable inputs used by the third party if such information is reasonably available to the entity.
Entities should make a reasonable effort to gather sufficient qualitative and quantitative information to determine whether fair value measurements based on third-party information are prepared in accordance with ASC 820 and to prepare applicable disclosures about fair value measurements. If, despite an entity’s efforts, quantitative information about significant unobservable inputs used by third-party pricing services is not reasonably available, the entity would not be required to create such information. Specifically, ASC 820-10-50-2(bbb)(2) states, in part:

A reporting entity is not required to create quantitative information to comply with this disclosure requirement if quantitative unobservable inputs are not developed by the reporting entity when measuring fair value (for example, when a reporting entity uses prices from prior transactions or third-party pricing information without adjustment). However, when providing this disclosure, a reporting entity cannot ignore quantitative unobservable inputs that are significant to the fair value measurement and are reasonably available to the reporting entity.

Notwithstanding this guidance, management must understand the information furnished by third-party service providers. If third-party service providers supply entities with details about the methods and assumptions used and with quantitative information to support the entity’s efforts to comply with the disclosure requirements in ASC 820, quantitative information about significant unobservable inputs may be reasonably available and should be disclosed.

Quantitative information about significant unobservable inputs used by a third party may become reasonably available to the entity in various ways, including, but not limited to:

- Recalculation of substantially all fair value measurements provided by third parties for a given class of asset or liability as part of the reporting entity’s process to ensure that these measurements are developed in accordance with ASC 820 or to comply with management’s responsibilities outlined in ASC 820-10-35-54K through 35-54M.11
- Inquiry and examination of supplemental information provided by third parties to either (1) comply with management’s responsibilities or (2) support a leveling disclosure (ASC 820-10-50-2(b)) and other required disclosures.

ASC 820 does not clearly address whether an other-than-nonpublic entity is subject to the requirement in ASC 820-10-50-2(g) to disclose qualitative information about the uncertainty of a Level 3 fair value measurement that results from the use of unobservable inputs when the entity does not also disclose quantitative information about significant unobservable inputs used by a third-party pricing service to develop the fair value measurement. In the absence of further clarification from standard setters or regulatory bodies, an entity should make a reasonable effort to disclose useful qualitative information about the uncertainty of a Level 3 fair value measurement that results from the use of unobservable inputs. Such information might be obtained as part of management’s process for understanding the valuation techniques and assumptions that the third party used in measuring fair value. See Section 10.8 for more information about management’s responsibilities when it uses fair value information provided by a third party.

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11 Note that entities are generally not required to disclose quantitative inputs about techniques that are used to validate other valuation techniques (e.g., secondary techniques that are not weighted in the fair value measurement).
### 11.2.3.5.1.4 Examples

ASC 820-10-55-103 and 55-104 illustrate the disclosure of quantitative information about significant unobservable inputs. Below is an additional example.

**Example 11-6**

**Disclosure of Quantitative Information About Significant Unobservable Inputs**

Entity D invests in various equity securities and RMBSs. In accordance with ASC 820-10-50-2B, D identifies three classes of equity securities, differentiating each class on the basis of the investees’ industry, and three classes of RMBSs based on the creditworthiness of underlying mortgage holders. (Note that an entity is not required to differentiate classes of debt investments on the basis of creditworthiness but should consider disaggregating classes when nature, characteristics, or risks differ in accordance with ASC 820-10-50-2B.) The following table presents the fair value by level within the fair value hierarchy for corresponding measurements as of December 31, 20X2:

<table>
<thead>
<tr>
<th>Description</th>
<th>Fair Value (000s)</th>
<th>Level 1</th>
<th>Level 2</th>
<th>Level 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity securities</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity securities — real estate industry</td>
<td>$ 93,000</td>
<td>$ 70,000</td>
<td>$ 23,000</td>
<td></td>
</tr>
<tr>
<td>Equity securities — oil and gas industry</td>
<td>45,000</td>
<td>45,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity securities — other</td>
<td>15,000</td>
<td>15,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total equity securities</strong></td>
<td><strong>153,000</strong></td>
<td><strong>130,000</strong></td>
<td>$ 23,000</td>
<td>$ —</td>
</tr>
<tr>
<td>Available-for-sale debt securities</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>RMBSs</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>RMBS — agency</td>
<td>36,000</td>
<td>24,000</td>
<td>12,000</td>
<td></td>
</tr>
<tr>
<td>RMBS — prime</td>
<td>7,000</td>
<td></td>
<td>7,000</td>
<td></td>
</tr>
<tr>
<td>RMBS — subprime</td>
<td>6,000</td>
<td></td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td>Commercial mortgage-backed securities</td>
<td>50,000</td>
<td></td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td><strong>Total available-for-sale debt securities</strong></td>
<td><strong>99,000</strong></td>
<td></td>
<td><strong>74,000</strong></td>
<td><strong>25,000</strong></td>
</tr>
<tr>
<td><strong>Total recurring fair value measurements</strong></td>
<td><strong>$ 252,000</strong></td>
<td><strong>130,000</strong></td>
<td><strong>$ 97,000</strong></td>
<td><strong>$ 25,000</strong></td>
</tr>
</tbody>
</table>

For the $25 million in Level 3 RMBSs, D uses unadjusted third-party information to measure the $16 million fair value of the RMBSs as follows: (1) $12 million of agency-backed RMBSs and (2) $4 million (of the $6 million) of subprime RMBSs. In preparing its fair value disclosures, D makes reasonable efforts to gather qualitative and quantitative information about the methods and assumptions used by third parties to price these RMBSs. Entity D concludes that it has sufficient information to comply with all other disclosure requirements but is not able to gather sufficient quantitative information about significant unobservable inputs used by third parties in their fair value measurements. Entity D has qualified for the disclosure exception in ASC 820-10-50-2(bbb)(2). Paragraph BC90 of ASU 2011-04 provides additional information on this issue.
Example 11-6 (continued)

For the remaining $9,000 of Level 3 RMBSs (i.e., the $7 million of prime RMBSs and $2 million of subprime RMBSs), D measures fair value on the basis of a discounted cash flow technique. The significant unobservable input in these Level 3 fair value measurements is the discount rate. Entity D uses multiple assumptions (i.e., underlying inputs) to develop the discount rates on these debt investments. Entity D performs the process described in Section 11.2.3.5.1.2 and determines that the following inputs underlying the discount rates are individually significant to each fair value measurement:

1. Level 2 risk-free interest rate based on U.S. Treasury yields.
2. Level 3 assumptions about prepayment speeds.
3. Level 3 assumptions about loss severities.
4. Level 3 assumptions about default rates.

Entity D separately discloses such inputs in accordance with ASC 820-10-50-2(bbb)(2) as follows:

<table>
<thead>
<tr>
<th>Asset</th>
<th>Fair Value (000s)</th>
<th>Valuation Technique(s)</th>
<th>Unobservable Input(s)</th>
<th>Low</th>
<th>High</th>
<th>Weighted Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>RMBS — agency</td>
<td>$ 12,000</td>
<td>Vendor pricing</td>
<td>Price</td>
<td>$ 102.00</td>
<td>$ 115.00</td>
<td>$ 104.00</td>
</tr>
<tr>
<td>RMBS — prime</td>
<td>$ 7,000</td>
<td>Discounted cash flow</td>
<td>Constant prepayment rate</td>
<td>0.00%</td>
<td>8.30%</td>
<td>2.30%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Loss severity</td>
<td>50.00%</td>
<td>70.00%</td>
<td>55.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Constant default rate</td>
<td>0.00%</td>
<td>18.00%</td>
<td>10.00%</td>
</tr>
<tr>
<td>RMBS — subprime</td>
<td>$ 2,000</td>
<td>Discounted cash flow</td>
<td>Constant prepayment rate</td>
<td>0.00%</td>
<td>10.00%</td>
<td>1.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Loss severity</td>
<td>60.00%</td>
<td>100.00%</td>
<td>80.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Constant default rate</td>
<td>0.00%</td>
<td>29.00%</td>
<td>18.00%</td>
</tr>
<tr>
<td>RMBS — subprime</td>
<td>$ 4,000</td>
<td>Vendor pricing</td>
<td>Price</td>
<td>$ 50.00</td>
<td>$ 65.00</td>
<td>$ 58.00</td>
</tr>
</tbody>
</table>

This presentation provides relevant information about the techniques and inputs used. In particular:

• Disclosing the fair value for measurements derived by using a given technique when multiple techniques were used makes it clear what technique was used to measure the fair value for respective portions of D’s RMBSs.
• Disaggregating the asset class gives users insight into the different assumptions used when risk and other characteristics differ.
• Disaggregating the discount rate into individually significant inputs increases the transparency of the assumptions used by management and the sources of potential uncertainty in the fair value measurements.
• Disclosing a weighted-average value for each input helps users understand the values applied to a majority of the securities in a given class. (Note that ASC 820-10-50-2(bbb)(2)(i) requires an other-than-nonpublic entity to disclose how it calculated the weighted average. Thus, D would also need to disclose how it calculated the weighted averages in the table above.)
11.2.3.5.2 Level 3 Fair Value Rollforward

11.2.3.5.2.1 General

As discussed in Section 11.2.2.1, ASC 820-10-50-2(c) requires other-than-nonpublic entities to disclose a “reconciliation from the opening balances to the closing balances” (i.e., beginning-of-period to end-of-period balances) for all classes of assets and liabilities measured at fair value on a recurring basis that are classified within Level 3 of the fair value hierarchy. In that reconciliation, the following must be disclosed in tabular format:

- “Total gains or losses for the period recognized in earnings” by income statement line item.
- “Total gains or losses for the period recognized” in OCI by line item in the statement of other comprehensive income.
- “Purchases, sales, issues, and settlements” (each of which is separately disclosed).
- The amount of transfers “into or out of Level 3 of the fair value hierarchy” and the reasons for those transfers (with transfers into Level 3 disclosed and discussed separately from transfers out of Level 3).

The example in ASC 820-10-55-101 illustrates how an entity might comply with this requirement.

ASC 820-10-50-2G states that, in lieu of providing the Level 3 rollforward, nonpublic entities “shall disclose separately changes during the period attributable to the following:

a. Purchases and issues (each of those types of changes disclosed separately)

b. The amounts of any transfers into or out of Level 3 of the fair value hierarchy and the reasons for those transfers. Transfers into Level 3 shall be disclosed and discussed separately from transfers out of Level 3.”

In paragraph BC71 of ASU 2018-13, the FASB acknowledged that users of nonpublic-entity financial statements “do not seek the same level of detailed information as users of public company financial statements” but that any information that “could signal an increase or decrease in the uncertainty of the fair value measurements” is relevant. The FASB believes that disclosing Level 3 purchases, issues, and transfers could enhance a user’s understanding of such uncertainty. Therefore, in lieu of applying ASC 820-10-50-2(c), nonpublic entities are subject to the disclosure requirements in ASC 820-10-50-2G.

11.2.3.5.2.2 Day 1 Gains or Losses

When the transaction price differs from the exit price at initial recognition of an asset or liability that is recognized at fair value on a recurring basis, an inception (or “day 1”) gain or loss is recognized in earnings. Other-than-nonpublic entities should include the impact of day 1 gains and losses in the Level 3 rollforward disclosure as well as in the disclosure required by ASC 820-10-50-2(d). A separate line item identifying the impact of day 1 gains or losses is not required unless an entity reports a “dealer profit” (i.e., day 1 gain) in an income statement line item separate from other gains and losses on derivatives. See Example 11-7 for a related illustration. Also see Section 9.2 for further discussion of when the transaction price differs from the exit price at initial recognition of an asset or liability.

---

12 Nonpublic entities are subject to the disclosure requirement in ASC 820-10-50-2G, with which they must comply in lieu of the Level 3 rollforward.
**Example 11-7**

**Impact of Day 1 Gain on Level 3 Rollforward**

Entity E, a broker-dealer, enters into a long-dated derivative contract with a counterparty in which it pays the counterparty $5 million at execution of the trade. However, E determines that it has not transacted in the principal (or most advantageous) market for the long-dated derivative (i.e., E can exit the long-dated derivative in the interdealer market at a higher price). Entity E determines that the fair value at inception is $8 million and that the inputs to the valuation of the long-dated derivative have a significant impact as a result of Level 3 inputs. At the end of the reporting period, E determines that the fair value of the long-dated derivative is $12 million (still with significant effects from Level 3 inputs). Entity E would provide the following disclosure regarding the long-dated derivative at the end of the period (in millions):

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Beginning Balance</strong></td>
<td>$ —</td>
</tr>
<tr>
<td>Total gains or losses (realized and unrealized):</td>
<td></td>
</tr>
<tr>
<td>(a) Recognized in earnings (included in other gain/loss*)</td>
<td>7</td>
</tr>
<tr>
<td>(b) Recognized in OCI (included in derivative gain/loss*)</td>
<td>—</td>
</tr>
<tr>
<td>Purchases</td>
<td>5</td>
</tr>
<tr>
<td>Sales</td>
<td>—</td>
</tr>
<tr>
<td>Issues</td>
<td>—</td>
</tr>
<tr>
<td>Settlements</td>
<td>—</td>
</tr>
<tr>
<td>Transfers into Level 3**</td>
<td>—</td>
</tr>
<tr>
<td>Transfers out of Level 3**</td>
<td>—</td>
</tr>
<tr>
<td><strong>Ending Balance</strong></td>
<td>$ 12</td>
</tr>
</tbody>
</table>

The amount of total gains or losses for the period recognized in earnings attributable to the change in unrealized gains or losses relating to assets still held at the end of the reporting period (included in other gain/loss*) $ 7

* A reporting entity is required to identify the line item in the statement of income or in the statement of comprehensive income (if applicable) in which the change in value, resulting from the fair value measurement, was recorded.

** A reporting entity is required to discuss the reasons for the transfers into and out of Level 3 and its policy for determining when such transfers have occurred.

Under ASC 820, E would not be required to separately identify the day 1 gain or loss (i.e., the $3 million profit at inception calculated as the difference between the $8 million fair value at inception and the $5 million transaction price) in the rollforward or supplemental disclosures unless it reports a “dealer profit” (i.e., day 1 gain) in a separate income statement line item. In either case, in the period of the transaction, the day 1 gain or loss is a component of the rollforward.
11.2.3.5.2.3 Derivatives

11.2.3.5.2.3.1 General

In preparing the Level 3 rollforward, an entity needs to take additional considerations into account for classes of assets and liabilities that meet the definition of a derivative instrument under ASC 815. Those considerations are explained below.

11.2.3.5.2.3.2 Determination of Gains and Losses on Financial and Physical Derivatives

ASC 820-10-50-2(c)(1) requires other-than-nonpublic entities to disclose “[t]otal gains or losses for the period recognized in earnings . . . and the line item(s) in the statement of income . . . in which those gains or losses are recognized,” and ASC 820-10-50-2(c)(1a) requires other-than-nonpublic entities to disclose “[t]otal gains or losses for the period recognized in other comprehensive income, and the line item(s) in other comprehensive income in which those gains or losses are recognized.” Further, ASC 815-10-50-4A through 50-4F require entities to provide separate disclosures about the location and amount of all gains and losses reported in the income statement for derivatives. Specifically, ASC 815-10-50-4A(b) requires the following disclosures:

The location and amount of the gains and losses on derivative instruments (and such nonderivative instruments) and related hedged items reported in any of the following:

1. The statement of financial performance
2. The statement of financial position (for example, gains and losses initially recognized in other comprehensive income).

The objectives of the gain and loss disclosure requirements of ASC 820 and ASC 815 are to provide information about the performance of an entity’s derivative instruments from an economic perspective (i.e., the impact of derivative instruments on the equity of the entity through net earnings or OCI).13 Neither the disclosure requirement in ASC 820-10-50-2(c)(1)/(c)(1a) nor that in ASC 815-10-50-4A(b) distinguishes between financially and physically settled derivatives (i.e., those that are settled gross through the receipt or delivery of the underlying asset in exchange for cash). Thus, the objectives of the gain and loss disclosure requirements for derivative instruments in ASC 820 are the same as those in ASC 815, regardless of whether the instruments are financially or physically settled. Moreover, although the scope of ASC 820-10-50-2(c)(1)/(c)(1a) is broader than that of ASC 815-10-50 in one respect (i.e., it applies to all recurring fair value measurements, not just derivative instruments) and narrower in another respect (i.e., it applies only to Level 3 measurements), the method an entity uses to determine the amount of gains or losses to disclose under ASC 820-10-50-2(c)(1)/(c)(1a) should be consistent with the method it uses to determine the amount of gains or losses under ASC 815-10-50-4A(b). ASC 815-10-50 implicitly suggests that the amount of gains and losses to be disclosed includes both realized and unrealized gains and losses, which is consistent with the disclosure requirement in ASC 820-10-50-2(c)(1) and (2)(c)(1a).

For financial derivatives, economic performance is demonstrated by the changes in fair value and resulting net settlements that occur over the life of the instrument. The determination of gains or losses on financial derivatives is based on the cash settlement activity. In contrast, physical fixed-price derivatives feature a gross exchange of an underlying asset (e.g., a physical commodity) and cash based on a pre-established price. However, the objective of the gain or loss disclosure remains the same — that is, to require entities to provide information about the performance of the derivative instrument from an economic perspective.

13 Paragraphs 82 and 83 of FASB Concepts Statement 6 define gains (or losses) as increases (or decreases) in “equity (net assets) from peripheral or incidental transactions of an entity and from all other transactions and other events and circumstances affecting the entity except those that result from revenues [or expenses] or investments by [or distributions to] owners.” Further, paragraph 87 states, “[p]re revenues and expenses are commonly displayed as gross inflows or outflows of net assets, while gains and losses are usually displayed as net inflows or outflows.”
For example, a physical fixed-price forward commodity contract economically consists of two elements: 14

1. A physical purchase or sale of the underlying commodity at the market price on the date of delivery. This results in a physical receipt or delivery of the commodity at its spot market price at the time of the settlement of the contract.

2. A financial fixed-price forward contract based on the same underlying commodity as the physical purchase or sale. This results in a hypothetical net cash settlement based on the difference between the spot market price of the commodity at the time of the settlement of the contract and the fixed price established by the physical derivative contract.

The second element’s change in fair value during the reporting period (i.e., the financial fixed-price forward contract) should be reflected as a gain or loss in the required disclosures. This approach achieves symmetry between financial and physical derivatives and provides financial statement users with relevant information about derivative performance.

Reflecting gross settlement amounts for physical derivatives in the settlement line of the ASC 820 Level 3 rollforward (i.e., the full settlement amount, including cash flows from the physical market purchase or sale element) would constitute an overstatement of gains or losses and would fail to reflect the economic impact of the contract on an entity’s equity. For example, a physical sale that is accounted for as a derivative instrument, that does not contain a financing element (e.g., that does not contain off-market terms or necessitate an up-front cash payment), and that is settled at the money (i.e., the spot market price equals the fixed price at the time of the settlement of the contract) does not result in any net economic benefit or detriment. An entity that enters any amount other than zero in the settlement line of the ASC 820 Level 3 rollforward would be required to increase or decrease another line of the reconciliation (presumably the gain or loss) to balance the reconciliation. However, reflecting the gross sales price established by the contract as a derivative gain would be a misrepresentation because it would ignore the fact that the entity delivered an asset of equal value. Likewise, a physical purchase that is accounted for as a derivative, that does not contain a financing element, and that is settled at the money does not result in an economic detriment, and reflecting the gross purchase price established by the contract as a derivative loss would be misrepresentative because the entity received an asset of equal value.

Example 11-8 illustrates the application of this guidance to financial derivatives and physical derivatives. In contemplating how gains or losses are determined and ultimately disclosed, an entity should also consider the guidance in ASC 820-10-50-2B and assess the appropriate classes of assets and liabilities for disclosure.

14 For simplicity, physical delivery risk (sometimes referred to as “index” risk), which is typically considered in the fair value calculation of a physical derivative, is not discussed here.
### Example 11-8

#### Financial Contract

<table>
<thead>
<tr>
<th></th>
<th>Financial Derivative 1</th>
<th>Financial Derivative 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning balance</td>
<td>$ 100</td>
<td>N/A — Entered into</td>
</tr>
<tr>
<td></td>
<td></td>
<td>during period</td>
</tr>
<tr>
<td>Change in fair value</td>
<td>10</td>
<td>$ 250</td>
</tr>
<tr>
<td>Cash received</td>
<td>110</td>
<td>N/A</td>
</tr>
<tr>
<td>Ending balance</td>
<td>—</td>
<td>$ 250</td>
</tr>
</tbody>
</table>

**Level 3 Rollforward**

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning balance</td>
<td>$ 100</td>
</tr>
<tr>
<td>Total gains or losses recognized in earnings (realized and unrealized)</td>
<td>260*</td>
</tr>
<tr>
<td>Transfers into Level 3</td>
<td>—</td>
</tr>
<tr>
<td>Transfers out of Level 3</td>
<td>—</td>
</tr>
<tr>
<td>Purchases</td>
<td>—</td>
</tr>
<tr>
<td>Sales</td>
<td>—</td>
</tr>
<tr>
<td>Issues</td>
<td>—</td>
</tr>
<tr>
<td>Settlements</td>
<td>(110)**</td>
</tr>
<tr>
<td>Ending balance</td>
<td>$ 250</td>
</tr>
</tbody>
</table>

* Represents change in fair value of derivative 1 ($10) and change in fair value of derivative 2 ($250).
** Represents cash received on settlement.

#### Physical Contract

<table>
<thead>
<tr>
<th></th>
<th>Physical Derivative 1</th>
<th>Physical Derivative 2</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(Sale of 100 MMBtu of Natural Gas at $8 per MMBtu)</td>
<td>(Sale of 100 MMBtu of Natural Gas at $12 per MMBtu)</td>
</tr>
<tr>
<td>Beginning balance</td>
<td>$ 100</td>
<td>N/A — Entered into during period</td>
</tr>
<tr>
<td>Change in fair value</td>
<td>10</td>
<td>$ 250</td>
</tr>
<tr>
<td>Cash received</td>
<td>800</td>
<td>N/A</td>
</tr>
<tr>
<td>Market value of commodity delivered</td>
<td>690</td>
<td>N/A</td>
</tr>
<tr>
<td>Ending balance</td>
<td>—</td>
<td>$ 250</td>
</tr>
</tbody>
</table>
Example 11-8 (continued)

<table>
<thead>
<tr>
<th>Level 3 Rollforward</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning balance</td>
</tr>
<tr>
<td>Total gains or losses recognized in earnings</td>
</tr>
<tr>
<td>Transfers into Level 3</td>
</tr>
<tr>
<td>Transfers out of Level 3</td>
</tr>
<tr>
<td>Purchases</td>
</tr>
<tr>
<td>Sales</td>
</tr>
<tr>
<td>Issues</td>
</tr>
<tr>
<td>Settlements</td>
</tr>
<tr>
<td>Ending balance</td>
</tr>
</tbody>
</table>

* Represents change in fair value of derivative 1 ($10) and change in fair value of derivative 2 ($250).

** Represents settlement of the financial fixed-price forward component of the physical derivative. The fixed price is the cash received on gross settlement ($800) that is offset against the spot market price for gas (underlying the physical derivative) at settlement. In this illustration, the spot price is assumed to be $6.90 per MMBtu or $690.

See Section 11.2.3.5.2.3.3 for discussion of how to determine the amounts of purchases, sales, issues, and settlements of derivative instruments that other-than-nonpublic entities must reflect in the Level 3 rollforward. (Note that nonpublic entities are only required to present purchases and issues of derivative instruments in accordance with ASC 820-10-50-2G.)

11.2.3.5.2.3.3 Determination of Purchases, Sales, Issues, and Settlements for Derivatives

ASC 820-10-50-2(c)(2) requires other-than-nonpublic entities to disclose “[p]urchases, sales, issues, and settlements (each of those types of changes disclosed separately)” as part of the Level 3 rollforward. Note that ASC 820-10-50-2G states that nonpublic entities are not required to complete Level 3 rollforward disclosures. Rather, in lieu of applying ASC 820-10-50-2(c), nonpublic entities must separately disclose changes during the period attributable to purchases and issues (each type separately) in accordance with ASC 820-10-50-2G(a).

When determining the amounts to disclose for individual derivative contracts for purchases, sales, issues, and settlements, an entity should evaluate the consideration exchanged (e.g., cash) between the counterparty and itself. However, an entity should not offset cash collateral receivables and payables with derivative assets and liabilities (see Section 11.2.3.5.2.3.5).

Typically, a derivative transaction that does not involve an up-front exchange of consideration (e.g., an at-market swap) should not be disclosed in the purchases, sales, or issues line items. Any ongoing payments under the contract would be reflected in the settlements line item. An up-front premium payment may not be required for an option acquired by an entity; instead, the entity may be required to make periodic premium payments to the counterparty over the term of the contract (i.e., the option premium is effectively financed by the counterparty). In this situation, the entity should consider the deferred premium payments as ongoing settlements rather than an up-front exchange of consideration, which the entity would typically present in the purchases line item.
The guidance below outlines the presentation of various types of payments related to derivative contracts within the Level 3 rollforward as purchases, sales, issues, or settlements.

- **Purchases** — An entity should present a derivative requiring an initial cash outlay (or other up-front consideration) in the purchases line item. Such presentation would include premium payments to purchase an option or up-front payments related to an off-market swap asset. Payments to acquire a derivative asset (through a contract assignment) should also be presented in the purchases line item.

- **Sales** — If an entity assigns a derivative asset to a third party for consideration, the payment should be presented in the sales line item. An assignment of a derivative liability should be disclosed as a settlement rather than as a sale (see the discussion in the “Settlements” bullet below for further details).

- **Issues** — If an entity executes a derivative and receives an initial cash inflow (or other up-front consideration), the up-front payment should be presented in the issues line item. In this situation, the entity has issued a derivative liability in return for consideration. Such presentation would include receipt of premium payments on written options or receipt of up-front payments related to an off-market swap liability. Payments received to assume a derivative contract liability (through a contract assignment) should also be presented in the issues line item and accompanied by separate disclosure describing the nature of the assignment transaction and the assignment amount related to the transaction. Alternatively, an entity may adopt a policy of presenting the consideration related to assignments of derivative liabilities in a separate line item other than purchases, sales, issues, or settlements, along with a disclosure describing the nature of the assignment transactions.

- **Settlements** — All ongoing contractual cash payments (or other consideration) made under the derivative contract should be disclosed in the settlements line item. Such disclosure would include payments on a multiperiod settled derivative (e.g., interest rate swaps that are net-cash-settled on a quarterly basis) or payments between the entity and counterparty to terminate a derivative or to exercise an option. In addition, if an entity assigns a derivative liability to a third party and is required to make a payment to the third party as part of the transaction, the payment should be presented in the settlements line item and accompanied by separate disclosure describing the nature of the assignment transaction and the settlement amount related to the transaction. An assignment of a derivative liability is akin to an early termination and thus a settlement of the original derivative. Alternatively, an entity may present the consideration related to assignments of derivative liabilities in a separate line item other than purchases, sales, issues, or settlements, along with a disclosure describing the nature of the assignment transactions.
Table 11-3 summarizes the application of ASC 820-10-50-2(c)(2) to various derivative transactions and highlights the concept of symmetry between the entity and counterparty.

### Table 11-3

<table>
<thead>
<tr>
<th>Transaction (From Reporting Entity’s Perspective)</th>
<th>Presentation by:</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchase of an option for up-front premium</td>
<td>Reporting Entity</td>
<td>Purchases</td>
<td>Counterparty (or Third-Party Assignee)</td>
</tr>
<tr>
<td>Writing of an option for up-front premium</td>
<td></td>
<td>Issues</td>
<td>Purchases</td>
</tr>
<tr>
<td>Assignment of derivative asset contract to a third party (assignee makes payment)</td>
<td></td>
<td>Sales</td>
<td>Purchases</td>
</tr>
<tr>
<td>Assignment of derivative liability contract to a third party (assignee receives payment)</td>
<td></td>
<td>Settlements*</td>
<td>Issues*</td>
</tr>
<tr>
<td>Periodic cash settlement of a swap contract</td>
<td></td>
<td>Settlements</td>
<td>Settlements</td>
</tr>
<tr>
<td>Early termination of derivative contract between parties to original contract</td>
<td></td>
<td>Settlements</td>
<td>Settlements</td>
</tr>
</tbody>
</table>

* If an entity adopts a policy of disclosing the consideration related to assignments of derivative liabilities as settlements (for assignments to third parties) or issues (for assignments from third parties), the entity should also include a separate disclosure describing the nature of the assignment transactions and the settlement amounts related to the transactions. Alternatively, an entity may adopt a policy of presenting the consideration related to assignments of derivative liabilities in a separate line item other than purchases, sales, issues, or settlements, along with a disclosure describing the nature of the assignment transactions. This policy should be disclosed and consistently applied.

Example 11-9 illustrates the application of this guidance to financial derivative instruments.

### Example 11-9

**Determination of Purchases, Sales, Issues, and Settlements for Financial Derivative Instruments**

Assume the following:

- **Financial Derivative 1** — Beginning balance of $100 asset; $10 change in fair value during period (i.e., increase in the fair value of the asset); termination cash payment of $110; zero ending balance.

- **Financial Derivative 2** — Beginning balance of $0; entity wrote a strip of interest rate caps and received consideration of $100; $500 change in fair value of derivative during period (i.e., increase in the fair value of the liability); one cap was exercised by the counterparty, for which a cash outflow of $75 during the period was required; ending derivative liability of $525.

- **Financial Derivative 3** — Beginning balance of $0; entity purchased an option for $50 up front; $30 change in fair value during period (decrease in the fair value of the asset); no settlement or exercise during the period; ending derivative asset of $20.

The entity has determined that Financial Derivative 1, Financial Derivative 2, and Financial Derivative 3 are separate classes (separate rollforwards are therefore required). See Section 11.2.3.1.2 for guidance on determining classes of derivative contracts.
### Example 11-9 (continued)

#### Level 3 Rollforward in Period 1*

<table>
<thead>
<tr>
<th>Financial Derivative 1</th>
<th>Financial Derivative 2</th>
<th>Financial Derivative 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning balance</td>
<td>$100</td>
<td>—</td>
</tr>
<tr>
<td>Total gains or (losses)</td>
<td>10</td>
<td>$(500)</td>
</tr>
<tr>
<td>Transfers</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Purchases</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Sales</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Issues</td>
<td>—</td>
<td>(100)</td>
</tr>
<tr>
<td>Settlements</td>
<td>(110)</td>
<td>75</td>
</tr>
<tr>
<td>Ending balance</td>
<td>—</td>
<td>$(525)</td>
</tr>
</tbody>
</table>

* Negative balances in the sales, issues, and settlements line items of this example represent cash inflows. The reconciliation is required to be presented not on a derivative-by-derivative basis but by class of derivative contract.

Assume the following additional facts (related to preparation of the disclosures for the second reporting period):

- **Financial Derivative 1** — Settled in prior period.
- **Financial Derivative 2** — Beginning liability balance of $525; $80 change in fair value of derivative during period (decrease in the fair value of the liability); no regular settlements during the period.
- **Financial Derivative 3** — Beginning asset balance of $20; $5 change in fair value during period (decrease in the fair value of the asset); no settlement or exercise during the period.

Upon downgrade of its credit rating by a rating agency, the entity is forced to terminate its entire portfolio of derivatives. The entity makes one cash payment of $430 to assign Financial Derivative 2 and Financial Derivative 3 to an independent third party.

#### Level 3 Rollforward in Period 2*

<table>
<thead>
<tr>
<th>Financial Derivative 2</th>
<th>Financial Derivative 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning balance</td>
<td>$ (525)</td>
</tr>
<tr>
<td>Total gains or (losses)</td>
<td>80</td>
</tr>
<tr>
<td>Transfers</td>
<td>—</td>
</tr>
<tr>
<td>Purchases</td>
<td>—</td>
</tr>
<tr>
<td>Sales</td>
<td>—</td>
</tr>
<tr>
<td>Issues</td>
<td>—</td>
</tr>
<tr>
<td>Settlements**</td>
<td>445</td>
</tr>
<tr>
<td>Ending balance</td>
<td>—</td>
</tr>
</tbody>
</table>

* Negative balances in the sales, issues, and settlements line items of this example represent cash inflows. The reconciliation is required to be presented not on a derivative-by-derivative basis but by class of derivative contract.

** The entity's accounting policy is to present the consideration paid to assign its derivative liabilities to third parties as settlements. The entity would also include a separate disclosure describing the nature of the assignment transaction and the settlement amount related to the transaction.
11.2.3.5.2.3.4 Gross Versus Net Presentation of Purchases, Sales, Issues, and Settlements for Derivatives

In accordance with ASC 820-10-50-2(c)(2), other-than-nonpublic entities must present, as part of the Level 3 rollforward, purchases, sales, issues, and settlements related to derivative instruments. ASC 820-10-50-3(b) addresses whether derivative assets and derivative liabilities must be presented on a gross or net basis in the Level 3 rollforward and allows entities to present derivative instruments on either a gross or net basis. Whether an entity chooses to present derivative instruments net (i.e., in one table) or gross (i.e., derivative assets and liabilities in two separate tables), the entity must still present purchases, sales, issues, and settlements separately for each class of derivative contract. That is, an entity that chooses to present derivative instruments on a net basis under ASC 820-10-50-3(b) is still required to separate the purchases, sales, issues, and settlements related to those derivatives in complying with the Level 3 rollforward requirement in ASC 820-10-50-2(c)(2). See also Examples 11-10 and 11-11.

Example 11-10

**Entity Purchases an Option and Writes an Option**

Assume the following:

- Entity F has a policy of presenting derivative contracts on a net basis in accordance with ASC 820-10-50-3(b).
- Entity F acquires an option for a $50 up-front payment and separately writes an option in return for a $100 up-front payment during the same period.
- In aggregating the fair value disclosures, F determines the class to be the same for each option.

It would not be appropriate for F to net the $50 purchase with the $100 issue and present a net $50 issue. Rather, F should, in the Level 3 rollforward, separately present the $50 purchase and $100 issue that occurred during the period.

Further assume that in a subsequent period, offsetting cash payments are made on these options. In this situation, because both option contracts are considered to be in the same class for aggregation purposes, F should net the subsequent payments associated with these contracts and present the net amount separately in the “settlements” line item.

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15 Nonpublic entities are not required to complete the Level 3 rollforward disclosure. However, in accordance with ASC 820-10-50-2G(a), they must still disclose purchases and issues (each type separately) for assets and liabilities classified within Level 3 of the fair value hierarchy.
Example 11-11

**Entity Assigns Derivative Asset and Derivative Liability**

Assume the following:

- Entity G chooses to present derivative contracts on a net basis in accordance with ASC 820-10-50-3(b).
- Entity G has a derivative asset with a fair value of $100 and a derivative liability with a fair value of $25.
- In aggregating the fair value disclosures, G determines the class to be the same for each derivative.
- During the period, G assigns the derivative asset and derivative liability to an independent third party in return for a cash payment of $75.

In this scenario, it would be acceptable for G to present the $75 payment received in the “sales” line item. Alternatively, G could allocate the $75 payment between the derivative asset and derivative liability and present these amounts separately in the Level 3 rollforward; the $100 related to the derivative asset would be presented in the sales line item, and the $25 related to the derivative liability would be presented in the settlements line item. Entity G could also present the derivative liability portion in a separate line item within the rollforward (e.g., a line item called “assignments of liabilities”). See Section 11.2.3.5.2.3.3 for additional guidance on presenting various types of payments related to derivative contracts within the Level 3 rollforward as purchases, sales, issues, or settlements. Regardless of the policy it selects, G should also include a separate disclosure describing the nature of the assignment transaction and the settlement amounts related to the transaction.

If G were instead to make a net payment to the third party in this example to assign a net derivative liability, G should present such a payment as a settlement. An allocation between the settlement of a derivative liability and sale of a derivative asset would also be acceptable.

11.2.3.5.2.3.5 Presentation of Cash Collateral Receivables and Payables

Under ASC 815-10-45-3 through 45-7, an entity may elect to offset, in its statement of financial position, fair value amounts recognized for its derivative instruments with fair value amounts recognized for the right or obligation to reclaim or return cash collateral (i.e., offset its derivative assets and liabilities with cash collateral receivables and payables). An entity that makes this election should not offset cash collateral receivables and payables with derivative assets and liabilities in ASC 820 disclosures, including the Level 3 rollforward. Although such fair value amounts are offset in the statement of financial position, such offsetting is inappropriate in the ASC 820 disclosures because doing so would be misleading. For example, assume that the net amount is the credit exposure under a particular master netting arrangement rather than the fair value amounts (measurements) of the derivative positions. Disclosure of the net amount would not allow financial statement users to identify the fair value amounts of the derivative instruments and where they are categorized in the fair value hierarchy. Example 11-12 illustrates an acceptable way of presenting the cash collateral receivables and payables in the ASC 820 disclosures.
Example 11-12

**Presentation of Cash Collateral on Derivative Instruments**

Cash collateral receivables and payables are presented in a separate column with other counterparty netting adjustments made under ASC 815-10-45-3 through 45-7. The entity uses the separate column to facilitate reconciliation with the balance sheet.

<table>
<thead>
<tr>
<th>Description</th>
<th>Quoted Prices in Active Markets for Identical Assets (Level 1)</th>
<th>Significant Other Observable Inputs (Level 2)</th>
<th>Significant Unobservable Inputs (Level 3)</th>
<th>Counterparty and Cash Collateral Netting</th>
<th>Amount Reported in the Balance Sheet as of 12/31/X8</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trading securities</td>
<td>$ 105</td>
<td>$ 10</td>
<td>$ 0</td>
<td>$ 0</td>
<td>$ 115</td>
</tr>
<tr>
<td>Derivative assets</td>
<td>$ 25</td>
<td>$ 15</td>
<td>$ 20</td>
<td>(15)*</td>
<td>45</td>
</tr>
<tr>
<td>Total assets</td>
<td>$ 130</td>
<td>$ 25</td>
<td>$ 20</td>
<td>(15)</td>
<td>$ 160</td>
</tr>
<tr>
<td>Derivative liabilities</td>
<td>$ 45</td>
<td>$ 65</td>
<td>$ 10</td>
<td>(35)*</td>
<td>85</td>
</tr>
<tr>
<td>Total liabilities</td>
<td>$ 45</td>
<td>$ 65</td>
<td>$ 10</td>
<td>(35)</td>
<td>85</td>
</tr>
</tbody>
</table>

* Amounts represent the effect of legally enforceable master netting arrangements between the reporting entity and its counterparties and the payable or receivable for cash collateral held or placed with the same counterparties.

Note that this presentation method for cash collateral receivables and payables and other counterparty netting adjustments made under ASC 815-10-45-3 through 45-7 does not apply in other circumstances (e.g., portfolio-level adjustments). See Section 11.2.3.5.5 for guidance on the allocation of portfolio-level adjustments.

11.2.3.5.3 Unrealized Gains and Losses on Level 3 Assets and Liabilities

ASC 820-10-50-2(d) requires other-than-nonpublic entities to separately disclose, for recurring fair value measurements categorized within Level 3 of the fair value hierarchy, “the amount of the total gains or losses for the period . . . included in earnings [or in comprehensive income] that is attributable to the change in unrealized gains or losses relating to those assets and liabilities held at the end of the reporting period, and the line item(s) . . . in which those unrealized gains or losses are recognized.”

In determining the unrealized portion of total gains or losses on Level 3 assets or liabilities held at the end of the reporting period, an entity should follow its established policy for determining when transfers between levels of the fair value hierarchy are deemed to have occurred (see Section 11.2.3.2.2) to ensure that amounts are reconciled to the amounts presented in the Level 3 rollforward (see Section 11.2.3.5.2). ASC 820-10-55-102 contains an example illustrating how an entity might separately disclose the unrealized portion of total gains and losses, by respective financial statement line item, as required by ASC 820-10-50-2(d).

In accordance with ASC 820-10-50-2F, nonpublic entities are not required to disclose the information required by ASC 820-10-50-2(d) unless another Codification topic requires them to do so.
11.2.3.5.4 Qualitative Uncertainty Disclosure for Level 3 Assets and Liabilities

ASC 820-10-50-2(g) requires other-than-nonpublic reporting entities to disclose “a narrative description of the uncertainty of [a] fair value measurement from the use of significant unobservable inputs if those inputs reasonably could have been different at the reporting date.” Entities should consider, at a minimum, the uncertainty of those unobservable inputs disclosed in accordance with ASC 820-10-50-2(bbb) when complying with this disclosure requirement and should also disclose any interrelationships between significant unobservable inputs that might exacerbate those measurement differences. The objective of such disclosure(s) is to help financial statement users understand not only the valuation techniques and inputs but also the judgments the entity uses when measuring fair value. See ASC 820-10-55-106 for further implementation guidance, including a sample disclosure about RMBSs.

In accordance with ASC 820-10-50-2F, nonpublic entities are not required to disclose the information required by ASC 820-10-50-2(g) unless another Codification topic requires them to do so.

11.2.3.5.5 Use of Net Risk Exception for Portfolio-Based Fair Value Measurements

Under ASC 820-10-35-18D, the fair value of a group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with ASC 815, or combinations of these items, can be measured on the basis of what would be received to exit a net-long or net-short risk position, provided that certain provisions are met. ASC 820-10-50-2D requires an entity to disclose the fact that it made an accounting policy decision to use the exception in ASC 820-10-35-18D. See Section 10.2.8 for further discussion of this valuation approach.

CVAs are commonly made at the portfolio level as long as the requirements outlined in ASC 820-10-35-18E through 35-18H are met. An entity might incorporate the effect of exposure to a particular counterparty’s credit by netting its derivative asset and liability contracts with a given counterparty in accordance with a master netting arrangement and then calculate a CVA on the basis of the net position with the counterparty. Thus, a CVA might apply to, and be calculated on the basis of, a portfolio of contracts that are individually classified in different levels of the fair value hierarchy. ASC 820-10-35-18L provides the following additional guidance about CVAs:

The reporting entity shall include the effect of the reporting entity's net exposure to the credit risk of that counterparty or the counterparty's net exposure to the credit risk of the reporting entity in the fair value measurement when market participants would take into account any existing arrangements that mitigate credit risk exposure in the event of default (for example, a master netting agreement with the counterparty or an agreement that requires the exchange of collateral on the basis of each party's net exposure to the credit risk of the other party). The fair value measurement shall reflect market participants' expectations about the likelihood that such an arrangement would be legally enforceable in the event of default.

As long as the requirements outlined in ASC 820-10-35-18E through 35-18H are met, mid-to-bid or mid-to-ask adjustments can also be made at the portfolio level. A derivatives dealer might initially use the midpoint in the bid-ask spread to value a portfolio of both its long (buys) and short (sells) derivative positions with the same underlying. The derivatives dealer would then make a mid-to-bid or mid-to-ask adjustment to effectively move the net open position of the portfolio to the bid or ask depending on whether the portfolio is net long or net short in each period. Thus, a mid-to-bid or mid-to-ask adjustment might apply to, and be calculated on the basis of, all of a portfolio’s derivative contracts that are individually classified in different levels of the fair value hierarchy. ASC 820-10-35-18I through 35-18K discuss additional considerations related to when an entity that uses the exception in ASC 820-10-35-18D is exposed to market risks and measures fair value.

16 Because some derivatives can be assets or liabilities depending on changes in market conditions, entities may employ more sophisticated techniques that factor in reasonably possible market fluctuations in determining the appropriate CVA. For simplicity, this guidance assumes that current exposure approximates expected exposure.
An entity must allocate portfolio-level adjustments to the individual assets and liabilities in complying with ASC 820's disclosure requirements. ASC 820-10-35-18G indicates the following:

A reporting entity shall make an accounting policy decision to use the exception in paragraph 820-10-35-18D. A reporting entity that uses the exception shall apply that accounting policy, including its policy for allocating bid-ask adjustments (see paragraphs 820-10-35-18I through 35-18K) and credit adjustments (see paragraph 820-10-35-18L), if applicable, consistently from period to period for a particular portfolio.

The ASC 820 disclosure requirements must be applied in a manner consistent with the asset's, liability's, or own equity instrument's unit of account (which is generally specified by Codification topics other than ASC 820). This is the case even when the ASC 820-10-35-18D exception has been applied. The unit of account under ASC 815 is each individual derivative. Accordingly, a CVA related to a portfolio of derivatives must be allocated to each individual derivative contract within the portfolio.

ASC 820 does not prescribe an approach for allocating portfolio-level adjustments to individual assets and liabilities. However, ASC 820-10-35-18G requires that an entity's policy be consistently applied. Entities must apply a reasonable method for allocating portfolio-level adjustments and should consider disclosing their policy in the notes to the financial statements.

An allocated portfolio adjustment is an input in the measurement of the fair value of the contract. Accordingly, an allocated portfolio adjustment that is a Level 3 input (i.e., either the portfolio adjustment or the allocation itself is unobservable) and that has a significant effect on the measurement of fair value of an individual asset, liability, or own equity instrument would cause the fair value of the entire individual asset, liability, or own equity instrument to be considered Level 3. Therefore, if a CVA is made on the basis of unobservable inputs, and that amount is allocated to individual derivative instruments within a portfolio, each individual derivative would represent a Level 3 fair value measurement solely on the basis of the CVA allocation if that allocation is significant to the measurement of this individual derivative instrument in its entirety.

### 11.3 Fair Value Disclosures — Before Adoption of ASU 2018-13

#### 11.3.1 Objectives and Scope

<table>
<thead>
<tr>
<th>ASC 820-10</th>
</tr>
</thead>
</table>
| **50-1** A reporting entity shall disclose information that helps users of its financial statements assess both of the following:

  a. For assets and liabilities that are measured at fair value on a recurring or nonrecurring basis in the statement of financial position after initial recognition, the valuation techniques and inputs used to develop those measurements

  b. For recurring fair value measurements using significant unobservable inputs (Level 3), the effect of the measurements on earnings (or changes in net assets) or other comprehensive income for the period. |
**ASC 820-10 (continued)**

**50-1A** To meet the objectives in the preceding paragraph, a reporting entity shall consider all of the following:

a. The level of detail necessary to satisfy the disclosure requirements
b. How much emphasis to place on each of the various requirements
c. How much aggregation or disaggregation to undertake
d. Whether users of financial statements need additional information to evaluate the quantitative information disclosed.

If the disclosures provided in accordance with this Topic and other Topics are insufficient to meet the objectives in the preceding paragraph, a reporting entity shall disclose additional information necessary to meet those objectives.

**50-1B** Paragraphs 820-10-55-99 through 55-107 illustrate disclosures about fair value measurements.

**50-2E** For each class of assets and liabilities not measured at fair value in the statement of financial position but for which the fair value is disclosed, a reporting entity shall disclose the information required by 820-10-50-2(b) and (h). . . .

**50-10** Plan assets of a defined benefit pension or other postretirement plan that are accounted for in accordance with Topic 715 are not subject to the disclosure requirements in paragraphs 820-10-50-1 through 50-9. Instead, the disclosures required in paragraphs 715-20-50-1(d)(iv) and 715-20-50-5(c)(iv) shall apply for fair value measurements of plan assets of a defined benefit pension or other postretirement plan.

**ASC 825-10**

**50-1** Paragraph 825-10-05-3 identifies various Topics within the Codification that address financial instrument matters. Those and other Topics in the Codification require disclosures about specific financial instruments. This Subsection addresses incremental disclosures about all of the following:

a. Fair value of financial instruments . . . .

**Applicability of This Subsection**

**50-2** This guidance discusses the applicability of the disclosure requirements in this Subsection to entities and transactions.

**Entities**

**50-2A** The disclosure guidance in this Subsection applies to public business entities . . . .
Chapter 11 — Disclosure

ASC 825-10 (continued)

Transactions

50-8 In part, this Subsection requires disclosures about fair value for all financial instruments, whether recognized or not recognized in the statement of financial position, except that the disclosures about fair value prescribed in paragraphs 825-10-50-10 through 50-13 and 825-10-50-15 are not required for any of the following:

a. Employers’ and plans’ obligations for pension benefits, other postretirement benefits including health care and life insurance benefits, postemployment benefits, employee stock option and stock purchase plans, and other forms of deferred compensation arrangements (see Topics 710, 712, 715, 718, and 960)

b. Substantively extinguished debt subject to the disclosure requirements of Subtopic 405-20

c. Insurance contracts, other than financial guarantees (including financial guarantee insurance contracts within the scope of Topic 944) and investment contracts, as discussed in Subtopic 944-20

d. Lease contracts as defined in Topic 840 [Topic 842] (a contingent obligation arising out of a cancelled lease and a guarantee of a third-party lease obligation are not lease contracts and are subject to the disclosure requirements in this Subsection)

e. Warranty obligations (see Topic 450 and the Product Warranties Subsections of Topic 460)

f. Unconditional purchase obligations as defined in paragraph 440-10-50-2

g. Investments accounted for under the equity method in accordance with the requirements of Topic 323

h. Noncontrolling interests and equity investments in consolidated subsidiaries (see Topic 810)

i. Equity instruments issued by the entity and classified in stockholders’ equity in the statement of financial position (see Topic 505)

j. Receive-variable, pay-fixed interest rate swaps for which the simplified hedge accounting approach is applied (see Topic 815)

k. Fully benefit-responsive investment contracts held by an employee benefit plan

l. Investments in equity securities accounted for under the measurement guidance for equity securities without readily determinable fair values (see Topic 321)

m. Trade receivables and payables due in one year or less

n. Deposit liabilities with no defined or contractual maturities

o. Liabilities resulting from the sale of prepaid stored-value products within the scope of paragraph 405-20-40-3.

50-9 Generally accepted accounting principles (GAAP) require disclosure of or subsequent measurement at fair value for many classes of financial instruments. Those requirements are not superseded or modified by this Subsection.

ASC 820 and ASC 825 require entities to disclose fair value information about the following assets and liabilities:

- Those that are measured at fair value in the statement of financial position in a financial reporting period after initial recognition (except for the plan assets of a defined benefit pension or other postretirement plan that is subject to the fair value disclosure requirements in ASC 715).

- Those that are not measured at fair value in the statement of financial position but for which the fair value is disclosed.
All assets and liabilities that are measured at fair value on a recurring or nonrecurring basis are subject to the disclosure requirements in ASC 820. An entity is not required to provide fair value disclosures for assets, liabilities, and instruments classified in a reporting entity’s shareholders’ equity that are initially recognized at fair value in accordance with ASC 820. However, other Codification topics may require specific fair value disclosures. See Chapter 2 for more information about the scope of ASC 820, including the application of the ASC 820 disclosure requirements to specific types of assets and liabilities. See Appendix A for a discussion of other Codification topics that require incremental fair value disclosures, including disclosures about fair value on initial recognition.

ASC 825 specifies the fair value disclosure requirements that apply to certain financial instruments, regardless of whether they are recognized in the statement of financial position. These disclosures, which only public business entities are required to provide, include disclosures about financial instruments that are not measured at fair value on a recurring or nonrecurring basis (e.g., financial assets and financial liabilities measured at amortized cost). ASC 825-10-50-8 provides exceptions from the disclosure requirements for certain financial instruments. See Chapter 2 for more information about the scope of ASC 825, including the application of its disclosure requirements to specific types of financial assets and financial liabilities.

ASC 820-10-50-1 and 50-1A outline the objective of the fair value disclosure requirements in ASC 820, along with matters for entities to consider in complying with these requirements. An entity may need to use significant judgment in determining the information to disclose and the level of detail (and aggregation or disaggregation) at which to provide such disclosures. In using such judgment, entities should consider the needs of present and potential investors, creditors, donors, and other financial statement users. Entities may determine that it is necessary to provide supplemental information (i.e., disclosures in addition to those required by ASC 820) in certain circumstances. See Section 11.3.3.1 for more information about determining classes of assets and liabilities for disclosure purposes.

**Connecting the Dots**

ASC 820-10-15-1 indicates that in the absence of a specific exception, “[ASC 820] applies when another [Codification topic] requires or permits fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements).” Thus, entities have the option of providing ASC 820 and ASC 825 disclosures for assets or liabilities for which such disclosures are not required. An entity may wish to disclose fair value information for certain assets and liabilities to give a more complete picture of their value or to provide supplemental information that is considered helpful to users of the entity’s financial statements.

There are various matters to consider regarding the voluntary disclosure of fair value information for assets and liabilities for which the disclosures in ASC 820 or ASC 825 are not required. Such considerations include the following:

- In addition to disclosing a fair value amount, an entity should consider the incremental disclosure requirements in ASC 820-10-50-2E for assets and liabilities not measured at fair value in the statement of financial position but for which the fair value is disclosed (see ASC 820-10-50-2(b) and ASC 820-10-50-2(h)). For such assets and liabilities, ASC 820-10-50-2E would not require the disclosure of other fair value information, such as the valuation technique, the inputs used in the valuation technique, quantitative disclosures about significant unobservable inputs for fair value amounts classified in Level 3 of the fair value hierarchy, and the valuation process for these amounts. However, entities can voluntarily include such disclosures for any asset or liability that is not measured at fair value in the statement of financial position.
• An entity should apply a rational and consistent policy when disclosing such fair value information (e.g., from one reporting period and asset or liability to another). The entity should also ensure that its disclosures clearly indicate that such assets and liabilities for which fair value is voluntarily disclosed are not recognized at fair value on a recurring or nonrecurring basis in the statement of financial position and should separately identify the associated carrying amounts reported in the statement of financial position. This is especially important when an entity has assets or liabilities of a similar type and some but not all of those assets or liabilities are recognized at fair value in the statement of financial position.

See Section 2.3.2.2.4 for discussion of voluntary fair value disclosures of equity method investments.

The remaining discussion in this section focuses on the disclosure requirements in ASC 820 and ASC 825 (for financial assets and financial liabilities of public business entities). Also see ASC 820-10-55-99 through 55-107 for examples illustrating disclosures that are not reproduced in the discussion below.

### 11.3.2 Disclosure Requirements

#### 11.3.2.1 Assets and Liabilities Measured at Fair Value in the Statement of Financial Position

**ASC 820-10**

50-2 To meet the objectives in paragraph 820-10-50-1, a reporting entity shall disclose, at a minimum, the following information for each class of assets and liabilities (see paragraph 820-10-50-2B for information on determining appropriate classes of assets and liabilities) measured at fair value (including measurements based on fair value within the scope of this Topic) in the statement of financial position after initial recognition:

a. For recurring fair value measurements, the fair value measurement at the end of the reporting period, and for nonrecurring fair value measurements, the fair value measurement at the relevant measurement date and the reasons for the measurement. Recurring fair value measurements of assets or liabilities are those that other Topics require or permit in the statement of financial position at the end of each reporting period. Nonrecurring fair value measurements of assets or liabilities are those that other Topics require or permit in the statement of financial position in particular circumstances (for example, when a reporting entity measures a long-lived asset or disposal group classified as held for sale at fair value less costs to sell in accordance with Topic 360 because the asset's fair value less costs to sell is lower than its carrying amount). For nonrecurring measurements estimated at a date during the reporting period other than the end of the reporting period, a reporting entity shall clearly indicate that the fair value information presented is not as of the period's end as well as the date or period that the measurement was taken.

b. For recurring and nonrecurring fair value measurements, the level of the fair value hierarchy within which the fair value measurements are categorized in their entirety (Level 1, 2, or 3). . .

bb. For assets and liabilities held at the end of the reporting period that are measured at fair value on a recurring basis, the amounts of any transfers between Level 1 and Level 2 of the fair value hierarchy, the reasons for those transfers, and the reporting entity's policy for determining when transfers between levels are deemed to have occurred (see paragraph 820-10-50-2C). Transfers into each level shall be disclosed and discussed separately from transfers out of each level. . .
ASC 820-10 (continued)

bbb. The information shall include:

1. For recurring and nonrecurring fair value measurements categorized within Level 2 and Level 3 of the fair value hierarchy, a description of the valuation technique(s) and the inputs used in the fair value measurement. If there has been a change in either or both a valuation approach and a valuation technique (for example, changing from matrix pricing to the binomial model or the use of an additional valuation technique), the reporting entity shall disclose that change and the reason(s) for making it.

2. For fair value measurements categorized within Level 3 of the fair value hierarchy, a reporting entity shall provide quantitative information about the significant unobservable inputs used in the fair value measurement. A reporting entity is not required to create quantitative information to comply with this disclosure requirement if quantitative unobservable inputs are not developed by the reporting entity when measuring fair value (for example, when a reporting entity uses prices from prior transactions or third-party pricing information without adjustment). However, when providing this disclosure, a reporting entity cannot ignore quantitative unobservable inputs that are significant to the fair value measurement and are reasonably available to the reporting entity. Employee benefit plans, other than those that are subject to the U.S. Securities and Exchange Commission's (SEC) filing requirements, are not required to provide this disclosure for investments held by an employee benefit plan in their plan sponsor's own nonpublic equity securities, including equity securities of their plan sponsor's nonpublic affiliated entities.

c. For recurring fair value measurements categorized within Level 3 of the fair value hierarchy, a reconciliation from the opening balances to the closing balances, disclosing separately changes during the period attributable to the following:

1. Total gains or losses for the period recognized in earnings (or changes in net assets), and the line item(s) in the statement of income (or activities) in which those gains or losses are recognized

   1a. Total gains or losses for the period recognized in other comprehensive income, and the line item(s) in other comprehensive income in which those gains or losses are recognized

2. Purchases, sales, issues, and settlements (each of those types of changes disclosed separately)

3. The amounts of any transfers into or out of Level 3 of the fair value hierarchy, the reasons for those transfers, and the reporting entity's policy for determining when transfers between levels are deemed to have occurred (see paragraph 820-10-50-2C). Transfers into Level 3 shall be disclosed and discussed separately from transfers out of Level 3.

d. For recurring fair value measurements categorized within Level 3 of the fair value hierarchy, the amount of the total gains or losses for the period in (c)(1) included in earnings (or changes in net assets) that is attributable to the change in unrealized gains or losses relating to those assets and liabilities held at the end of the reporting period, and the line item(s) in the statement of income (or activities) in which those unrealized gains or losses are recognized.

f. For recurring and nonrecurring fair value measurements categorized within Level 3 of the fair value hierarchy, a description of the valuation processes used by the reporting entity (including, for example, how an entity decides its valuation policies and procedures and analyzes changes in fair value measurements from period to period). See paragraph 820-10-55-105 for further guidance.

g. For recurring fair value measurements categorized within Level 3 of the fair value hierarchy, a narrative description of the sensitivity of the fair value measurement to changes in unobservable inputs if a change in those inputs to a different amount might result in a significantly higher or lower fair value measurement. If there are interrelationships between those inputs and other unobservable inputs used in the fair value measurement, a reporting entity shall also provide a description of those interrelationships and of how they might magnify or mitigate the effect of changes in the unobservable inputs on the fair value measurement. To comply with that disclosure requirement, the narrative description of the sensitivity to changes in unobservable inputs shall include, at a minimum, the unobservable inputs disclosed when complying with paragraph 820-10-50-2(bbb).

h. For recurring and nonrecurring fair value measurements, if the highest and best use of a nonfinancial asset differs from its current use, a reporting entity shall disclose that fact and why the nonfinancial asset is being used in a manner that differs from its highest and best use.
### ASC 820-10 (continued)

<table>
<thead>
<tr>
<th>Paragraph</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>50-2B</td>
<td>A class of assets and liabilities will often require greater disaggregation than the line items presented in the statement of financial position. However, a reporting entity shall provide information sufficient to permit reconciliation to the line items presented in the statement of financial position. . . .</td>
</tr>
</tbody>
</table>
| 50-2C     | A reporting entity shall disclose and consistently follow its policy for determining when transfers between levels of the fair value hierarchy are deemed to have occurred in accordance with paragraph 820-10-50-2(bb) and (c)(3). The policy about the timing of recognizing transfers shall be the same for transfers into the levels as for transfers out of the levels. Examples of policies for determining the timing of transfers include the following:  
  a. The date of the event or change in circumstances that caused the transfer  
  b. The beginning of the reporting period  
  c. The end of the reporting period. |
| 50-2D     | If a reporting entity makes an accounting policy decision to use the exception in paragraph 820-10-35-18D, it shall disclose that fact. |
| 50-2F     | A nonpublic entity is not required to disclose the information required by paragraph 820-10-50-2(bb) and (g) and paragraph 820-10-50-2E unless required by another Topic. |
| 50-3      | For derivative assets and liabilities, the reporting entity shall present both of the following:  
  a. The fair value disclosures required by paragraph 820-10-50-2(a) through (bb) on a gross basis (which is consistent with the requirement of paragraph 815-10-50-4B(a))  
  b. The reconciliation disclosure required by paragraph 820-10-50-2(c) through (d) on either a gross or a net basis. |
| 50-4A     | For a liability measured at fair value and issued with an inseparable third-party credit enhancement, an issuer shall disclose the existence of that credit enhancement. |
| 50-7      | As discussed in paragraph 250-10-50-5, the disclosures required by Topic 250 for a change in accounting estimate are not required for revisions resulting from a change in a valuation technique or its application. |
| 50-8      | A reporting entity shall present the quantitative disclosures required by this Topic in a tabular format. |

All assets and liabilities measured in the statement of financial position at fair value after initial recognition are subject to the disclosure requirements in ASC 820-10-50-2. The nature and extent of such disclosures differ depending on the following:  
- Whether the reporting entity is a nonpublic entity (see Section 11.1.3).  
- Whether the fair value measurement is recurring or nonrecurring (see Section 11.1.5).  

Table 11-4 summarizes the disclosures an entity is required to provide under ASC 820 when, in accordance with other Codification topics, an asset or liability is measured at fair value in the statement of financial position after initial recognition. This table distinguishes between (1) other-than-nonpublic and nonpublic entities and (2) recurring and nonrecurring fair value measurements. As noted in ASC 820-10-50-8, the quantitative disclosures must be presented in a tabular format. See the remaining subsections of Section 11.3 for more information about these required disclosures.
Table 11-4

<table>
<thead>
<tr>
<th>Required Disclosures and Applicable References</th>
<th>Entities Other Than Nonpublic Entities</th>
<th>Nonpublic Entities</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Recurring</td>
<td>Nonrecurring</td>
</tr>
<tr>
<td>Fair value as of the reporting date or relevant measurement date (ASC 820-10-50-2(a) and ASC 825-10-50-10)</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>The reason for the fair value measurement (ASC 820-10-50-2(a))</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>The level in the fair value hierarchy (ASC 820-10-50-2(b) and ASC 825-10-50-10)</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>The amounts of any transfers between Levels 1 and 2, the reasons for those transfers, and the entity's policy for determining whether a transfer has occurred; transfers into each level would be disclosed and discussed separately from transfers out of each level (ASC 820-10-50-2(bb))</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>For fair value measurements in Levels 2 and 3 of the fair value hierarchy, a description of the valuation techniques and inputs used in the fair value measurement (ASC 820-10-50-2(bbb)(1))</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>For fair value measurements in Levels 2 and 3 of the fair value hierarchy, if there has been a change in a valuation approach, a valuation technique, or both, the nature of, and reason for, that change (ASC 820-10-50-2(bbb)(1))</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>If the highest and best use of a nonfinancial asset differs from its current use, disclosure of that fact and why the asset is being used in such a way (ASC 820-10-50-2(h))</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Information sufficient to permit reconciliation of (1) disclosures about classes of assets and liabilities by level in the fair value hierarchy and (2) line items presented in the statement of financial position (ASC 820-10-50-2B)</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>The policy for determining when transfers between levels of the fair value hierarchy have occurred in accordance with ASC 820-10-50-2(bb) through 50-2(c)(3)</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>If an entity makes an accounting policy decision to use the net risk position valuation exception in ASC 820-10-35-18D, disclosure of that fact (ASC 820-10-50-2D)</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>For liabilities measured at fair value, the existence of any credit enhancement and whether it is reflected in the fair value measurement (ASC 820-10-50-4A)</td>
<td>X</td>
<td>X</td>
</tr>
</tbody>
</table>
### Required Disclosures and Applicable References

<table>
<thead>
<tr>
<th>The disclosures below apply only to Level 3 fair value measurements.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Entities Other Than Nonpublic Entities</strong></td>
</tr>
<tr>
<td><strong>Nonpublic Entities</strong></td>
</tr>
<tr>
<td><strong>Recurring</strong></td>
</tr>
<tr>
<td>Quantitative information about the significant unobservable inputs used in the fair value measurement (ASC 820-10-50-2(bbb)(2))</td>
</tr>
<tr>
<td>The Level 3 rollforward (ASC 820-10-50-2(c))</td>
</tr>
<tr>
<td>The total amount of gains and losses for the period, recorded in current income, that is attributable to the change in unrealized gains and losses for assets or liabilities held at the end of the reporting period and the line items in which such amounts are recognized (ASC 820-10-50-2(d))</td>
</tr>
<tr>
<td>Description of the valuation processes used by the entity, including a discussion of how the entity decides its policies and procedures and analyzes changes in fair value from period to period (ASC 820-10-50-2(f))</td>
</tr>
<tr>
<td>Narrative description of the sensitivity of the fair value measurement to changes in unobservable inputs (i.e., those disclosed in ASC 820-10-50-2(bbb)), if a change in those inputs to a different amount might result in a significantly different fair value measurement, and a description of the interrelationships between unobservable inputs, including how such relationships might magnify or mitigate the impact of changes in such inputs on fair value (ASC 820-10-50-2(g))</td>
</tr>
</tbody>
</table>

### Notes to table:

(a) ASC 820-10-50-2(a) requires disclosure of a nonrecurring fair value measurement amount as of the date of the measurement (e.g., the impairment or recovery date), which may differ from the end of the reporting period. ASC 820-10-50-2(a) states, in part, “[f]or nonrecurring measurements estimated at a date during the reporting period other than the end of the reporting period, a reporting entity shall clearly indicate that the fair value information presented is not as of the period’s end as well as the date or period that the measurement was taken.” ASC 820-10-50-2B further states, in part, that “a reporting entity shall provide information sufficient to permit reconciliation to the line items presented in the statement of financial position.” These disclosure requirements address situations for which the amounts disclosed under ASC 820 for assets or liabilities measured at fair value on a nonrecurring basis during the period are not consistent with the amounts recorded in the statement of financial position for such assets or liabilities. See also Section 11.3.3.3.2.

(b) ASC 820-10-50-2F exempts nonpublic entities from providing this disclosure unless it is required by another Codification topic.

(c) ASC 820-10-50-2F exempts nonpublic entities from providing this disclosure because it pertains to transfers between Level 1 and Level 2 of the fair value hierarchy.

(d) ASC 820-10-50-2(bbb)(2) states, in part:

    A reporting entity is not required to create quantitative information to comply with this disclosure requirement if quantitative unobservable inputs are not developed by the reporting entity when measuring fair value (for example, when a reporting entity uses prices from prior transactions or third-party pricing information without adjustment). However, when providing this disclosure, a reporting entity cannot ignore quantitative unobservable inputs that are significant to the fair value measurement and are reasonably available to the reporting entity. Employee benefit plans, other than those plans that are subject to the U.S. Securities and Exchange Commission’s (SEC) filing requirements, are not required to provide this disclosure for investments held by an employee benefit plan in their plan sponsor’s own nonpublic equity securities, including equity securities of their plan sponsor’s nonpublic affiliated entities.
(Table continued)

(e) This disclosure is not required for fair value measurements related to the financial accounting and reporting for goodwill after its initial recognition (see ASC 350-20-50-3).

(f) For nonpublic entities, this disclosure is not required for fair value measurements related to the financial accounting and reporting for (1) goodwill after its initial recognition (see ASC 350-20-50-3) and (2) indefinite-lived intangible assets after their initial recognition (see ASC 350-30-50-3A).

See ASC 820-10-50-3 for additional disclosure requirements related to derivative assets and liabilities.

SEC Considerations

Section 9700 of the FRM states:

In March and September 2008, the Division of Corporation Finance sent illustrative letters to certain public companies that reported significant amounts of asset-backed securities, loans carried at fair value or the lower of cost or market, and derivative assets and liabilities in their recent 10-K filings. The letters highlight disclosure matters relating to SFAS 157 [ASC 820], and suggest disclosures that companies may consider in preparing their MD&A.

These letters highlight disclosure matters that SEC registrants should consider in complying with SEC Regulation S-K, Item 303, which addresses the preparation of MD&A. While certain of the recommended disclosures are now required under U.S. GAAP as a result of amendments to ASC 820, SEC registrants should consider the disclosures suggested in these letters that are not otherwise provided in the notes to the financial statements.

11.3.2.2 Assets and Liabilities Not Measured at Fair Value in the Statement of Financial Position

<table>
<thead>
<tr>
<th>ASC 820-10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>50-2E</strong> For each class of assets and liabilities not measured at fair value in the statement of financial position but for which the fair value is disclosed, a reporting entity shall disclose the information required by paragraph 820-10-50-2(b) and (h). However, a reporting entity is not required to provide the quantitative disclosures about significant unobservable inputs used in fair value measurements categorized within Level 3 of the fair value hierarchy required by paragraph 820-10-50-2(bbb)(2). For such assets and liabilities, a reporting entity does not need to provide the other disclosures required by this Topic.</td>
</tr>
<tr>
<td><strong>50-2F</strong> A nonpublic entity is not required to disclose the information required by paragraph 820-10-50-2(bb) and (g) and paragraph 820-10-50-2E unless required by another Topic.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>ASC 825-10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Entities</strong></td>
</tr>
<tr>
<td><strong>50-2A</strong> The disclosure guidance in this Subsection applies to public business entities. . . .</td>
</tr>
<tr>
<td><strong>50-9</strong> Generally accepted accounting principles (GAAP) require disclosure of or subsequent measurement at fair value for many classes of financial instruments. Those requirements are not superseded or modified by this Subsection.</td>
</tr>
<tr>
<td><strong>50-10</strong> A reporting entity shall disclose either in the body of the financial statements or in the accompanying notes, the fair value of financial instruments and the level of the fair value hierarchy within which the fair value measurements are categorized in their entirety (Level 1, 2, or 3). . . .</td>
</tr>
</tbody>
</table>

For financial instruments recognized at fair value in the statement of financial position, the disclosure requirements of Topic 820 also apply.
<table>
<thead>
<tr>
<th><strong>ASC 825-10 (continued)</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>50-11</strong> Fair value disclosed in the notes shall be presented together with the related carrying amount in a form that clarifies both of the following:</td>
</tr>
<tr>
<td>a. Whether the fair value and carrying amount represent assets or liabilities</td>
</tr>
<tr>
<td>b. How the carrying amounts relate to what is reported in the statement of financial position.</td>
</tr>
<tr>
<td><strong>50-12</strong> If the fair value of financial instruments is disclosed in more than a single note, one of the notes shall include a summary table. The summary table shall contain the fair value and related carrying amounts and cross-references to the location(s) of the remaining disclosures required by this Section.</td>
</tr>
<tr>
<td><strong>50-13</strong> This Subtopic does not prohibit an entity from disclosing separately the estimated fair value of any of its nonfinancial intangible and tangible assets and nonfinancial liabilities.</td>
</tr>
<tr>
<td><strong>50-15</strong> In disclosing the fair value of a financial instrument, an entity shall not net that fair value with the fair value of other financial instruments — even if those financial instruments are of the same class or are otherwise considered to be related (for example, by a risk management strategy) — except to the extent that the offsetting of carrying amounts in the statement of financial position is permitted under either of the following:</td>
</tr>
<tr>
<td>a. The general principle in paragraph 210-20-45-1</td>
</tr>
<tr>
<td>b. The exceptions for master netting arrangements in paragraph 815-10-45-5 and for amounts related to certain repurchase and reverse repurchase agreements in paragraphs 210-20-45-11 through 45-17.</td>
</tr>
</tbody>
</table>

Public business entities must provide additional fair value disclosures for certain financial assets and financial liabilities that are not measured at fair value in the statement of financial position, which may include financial assets or financial liabilities that were subject to a nonrecurring fair value measurement during a financial reporting period. This disclosure requirement is included in ASC 825-10-50-10 and is also addressed in ASC 820-10-50-2E. In accordance with that guidance, public business entities must disclose the following for financial assets and financial liabilities that are not (1) recognized at fair value in the statement of financial position and (2) subject to an exception in ASC 825-10-50-8:

- The fair value as of the reporting date (i.e., the date of the statement of financial position).
- The level of the fair value hierarchy (Level 1, 2, or 3) within which each fair value measurement is categorized in its entirety.\(^\text{17}\)

These disclosures can be included in the body of the financial statements or in the notes and may be provided by classes of assets and liabilities (see Section 11.3.3.1), subject to the prohibitions against netting described in ASC 825-10-50-15. ASC 825-10-50-11 and 50-12 address considerations related to including such disclosures in the notes to the financial statements.

The fair value disclosures should be consistent with the unit of account. For example, as discussed in ASC 825-10-25-13, “[f]or the issuer of a liability issued with an inseparable third-party credit enhancement . . . the unit of accounting for the liability . . . disclosed at fair value does not include the third-party credit enhancement.”

While an entity is not precluded from also disclosing information about the valuation technique and inputs used, changes in the valuation approach or valuation technique, and significant unobservable inputs, these disclosures are not required for financial assets and financial liabilities that are not

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\(^{17}\) ASC 820-10-50-2E also refers to the disclosure requirement in ASC 820-10-50-2(h). However, since public business entities are not required to disclose the fair value of nonfinancial assets that are not recognized at fair value, it is unlikely that this disclosure will be relevant to the disclosure of the fair values of items not recognized at fair value.
measured at fair value in the statement of financial position. ASU 2018-09 clarified that the disclosure addressed in ASC 820-10-50-2(bbb) is not required for financial assets and financial liabilities that are not measured at fair value.

Entities other than public business entities are not required to provide disclosures about the fair value of financial assets and financial liabilities that are not measured at fair value in the statement of financial position. Further, ASU 2019-04 clarified that such entities do not need to disclose the fair values of held-to-maturity classified debt securities.

See Section 11.4 for examples of financial instruments that are subject to the disclosure requirements of ASC 825-10-50-10.

### 11.3.2.3 Certain Entities That Calculate NAV per Share (or Its Equivalent)

<table>
<thead>
<tr>
<th>ASC 820-10</th>
</tr>
</thead>
</table>

**Fair Value Measurements of Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)**

50-6A For investments that are within the scope of paragraphs 820-10-15-4 through 15-5 and that are measured using the practical expedient in paragraph 820-10-35-59 on a recurring or nonrecurring basis during the period, a reporting entity shall disclose information that helps users of its financial statements to understand the nature and risks of the investments and whether the investments, if sold, are probable of being sold at amounts different from net asset value per share (or its equivalent, such as member units or an ownership interest in partners' capital to which a proportionate share of net assets is attributed). To meet that objective, to the extent applicable, a reporting entity shall disclose, at a minimum, the following information for each class of investment:

a. The fair value measurement (as determined by applying paragraphs 820-10-35-59 through 35-62) of the investments in the class at the reporting date and a description of the significant investment strategies of the investee(s) in the class.

b. For each class of investment that includes investments that can never be redeemed with the investees, but the reporting entity receives distributions through the liquidation of the underlying assets of the investees, the reporting entity's estimate of the period of time over which the underlying assets are expected to be liquidated by the investees.

c. The amount of the reporting entity's unfunded commitments related to investments in the class.

d. A general description of the terms and conditions upon which the investor may redeem investments in the class (for example, quarterly redemption with 60 days' notice).

e. The circumstances in which an otherwise redeemable investment in the class (or a portion thereof) might not be redeemable (for example, investments subject to a lockup or gate). Also, for those otherwise redeemable investments that are restricted from redemption as of the reporting entity's measurement date, the reporting entity shall disclose its estimate of when the restriction from redemption might lapse. If an estimate cannot be made, the reporting entity shall disclose that fact and how long the restriction has been in effect.

f. Any other significant restriction on the ability to sell investments in the class at the measurement date.

h. If a group of investments would otherwise meet the criteria in paragraph 820-10-35-62 but the individual investments to be sold have not been identified (for example, if a reporting entity decides to sell 20 percent of its investments in private equity funds but the individual investments to be sold have not been identified), so the investments continue to qualify for the practical expedient in paragraph 820-10-35-59, the reporting entity shall disclose its plans to sell and any remaining actions required to complete the sale(s).
Chapter 11 — Disclosure

ASC 820-10-35-59 permits entities, as a practical expedient, to estimate the fair value of an investment within the scope of ASC 820-10-15-4 and 15-5 by using the NAV per share (or its equivalent, such as member units or an ownership interest in partners' capital to which a proportionate share of net assets is attributed) of the investment, provided that it is calculated in a manner consistent with the measurement principles of ASC 946 as of the reporting entity’s measurement date. To help financial statement users understand the nature and risks of the investments and whether it is probable that they will be sold (if they are sold) at amounts that differ from the NAV per share (or its equivalent), ASC 820-10-50-6A requires specific disclosures, for each interim and annual period, for investment classes within the scope of ASC 820-10-15-4 and 15-5 that an entity measured during the period on a recurring or nonrecurring basis by using the practical expedient in ASC 820-10-35-59. See ASC 820-10-55-107 for an example illustrating such disclosures.

Although investments that an entity records when using the practical expedient in ASC 820-10-35-59 are not categorized within the fair value hierarchy, ASC 820-10-35-54B still requires an entity to provide the amounts that it measured by using the practical expedient so that the fair value of investments included in the fair value hierarchy can be reconciled to the line items presented in the statement of financial position in accordance with ASC 820-10-50-2B.

Entities are not required to apply the practical expedient in ASC 820-10-35-59 to all investments within the scope of ASC 820-10-15-4 and 15-5. When the practical expedient is not used for such investments, the disclosures outlined in ASC 820-10-50-6A are not required. Rather, as stated in paragraph BC11 of ASU 2015-07, “the fair value of the investment will be included in the fair value hierarchy on the basis of the relative observability of the inputs used in the valuation and subject to the disclosure requirements of paragraph 820-10-50-2.”

11.3.3 Interpretive Guidance

11.3.3.1 Identifying Classes of Assets and Liabilities

11.3.3.1.1 General

<table>
<thead>
<tr>
<th>ASC 820-10</th>
</tr>
</thead>
<tbody>
<tr>
<td>50-2B A reporting entity shall determine appropriate classes of assets and liabilities on the basis of the following:</td>
</tr>
<tr>
<td>a. The nature, characteristics, and risks of the asset or liability</td>
</tr>
<tr>
<td>b. The level of the fair value hierarchy within which the fair value measurement is categorized.</td>
</tr>
</tbody>
</table>

The number of classes may need to be greater for fair value measurements categorized within Level 3 of the fair value hierarchy because those measurements have a greater degree of uncertainty and subjectivity. Determining appropriate classes of assets and liabilities for which disclosures about fair value measurements should be provided requires judgment. A class of assets and liabilities will often require greater disaggregation than the line items presented in the statement of financial position. However, a reporting entity shall provide information sufficient to permit reconciliation to the line items presented in the statement of financial position. If another Topic specifies the class for an asset or a liability, a reporting entity may use that class in providing the disclosures required in this Topic if that class meets the requirements in this paragraph.

In complying with the fair value disclosure requirements of ASC 820-10-50-2, an entity must determine appropriate classes of assets and liabilities in accordance with ASC 820-10-50-2B. An entity must use judgment and carefully consider the facts and circumstances in disaggregating assets and liabilities into separate classes. Such disaggregation often results in a more granular presentation for fair value.

See Sections 2.2.2 and 10.9 for further discussion of this practical expedient.
When determining the appropriate level of disaggregation into classes of assets and liabilities, entities should consider the nature, characteristics, and risk profile of the assets and liabilities, as well as the level of the fair value hierarchy within which each fair value measurement has been categorized. Entities may also consider guidance in other Codification topics (e.g., ASC 320, ASC 815) when making this determination. ASC 320-10-50-1B provides guidance on class determination and useful considerations related to assessing the nature of and risks associated with debt securities. On the basis of those requirements, concentrations are likely to be important in the determination of class for all assets and liabilities.

When preparing quantitative disclosures about significant unobservable inputs used in Level 3 fair value measurements, an entity may discover that:

- Different techniques are used for individual assets, liabilities, or subclasses within a previously identified class of asset or liability.
- Different inputs are being used even when the same technique is used to measure different assets, liabilities, or subclasses within a class.
- The quantitative information varies significantly between one asset, liability, or subclass and others within a class.

Such differences may indicate that the nature, characteristics, or risks of assets, liabilities, or subclasses within a previously identified class differ and that it would be appropriate to create more classes. When disaggregating an asset or liability class because techniques, inputs, or quantitative information about inputs differs, an entity should consider disaggregating the class in other disclosures required by ASC 820-10-50-2(a)–(h) to ensure consistency.

An entity that does not use the same classes throughout its fair value disclosures should consider reconciling, for example, the classes of assets and liabilities categorized in Level 3 of the fair value hierarchy between the leveling disclosures (see ASC 820-10-50-2(b)) and the quantitative disclosures about significant unobservable inputs (see ASC 820-10-50-2(bbb)(2)). Entities should also keep in mind the requirement from ASC 820-10-50-2B to “provide information sufficient to permit reconciliation to the line items presented in the statement of financial position.”
The following examples illustrate disaggregation of assets into classes by using various approaches:

### Example 11-13

**Aggregation by Valuation Technique**

Entity A holds RMBSs backed by both prime (i.e., higher credit quality) and subprime (i.e., lower credit quality) mortgages. When identifying the class of asset for disclosure purposes, A concludes that the nature, risks, and characteristics (including valuation technique) of these assets are sufficiently similar to allow aggregation of all RMBSs into one class. Entity A prepares the disclosure below. However, if A holds material amounts of RMBSs backed by mortgages of significantly differing credit quality, this disclosure may not provide sufficient information for financial statement users to understand and evaluate the quantitative information provided. In such a case, A could consider an alternative such as the one presented in Example 11-14.

<table>
<thead>
<tr>
<th>Asset</th>
<th>Fair Value (000s)</th>
<th>Valuation Technique(s)</th>
<th>Unobservable Input(s)</th>
<th>Low</th>
<th>High</th>
<th>Weighted Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>RMBS</td>
<td>$ 9,000</td>
<td>Discounted cash flow</td>
<td>Constant prepayment rate</td>
<td>0.00%</td>
<td>10.00%</td>
<td>2.01%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Loss severity</td>
<td>50.00%</td>
<td>100.00%</td>
<td>60.56%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Constant default rate</td>
<td>0.00%</td>
<td>29.00%</td>
<td>11.78%</td>
</tr>
</tbody>
</table>

### Example 11-14

**Disaggregation by Risk**

This presentation alternative results in more relevant information for financial statement users than the approach in Example 11-13, enabling them to better understand and evaluate the techniques and inputs used. In particular, disaggregating the asset class gives users insight into the different assumptions used when risk and other characteristics differ. Because the guidance that applies to determination of class for this disclosure is the same as the guidance that applies to determination of class for a disclosure of fair value by level in the fair value hierarchy (i.e., the requirement in ASC 820-10-50-2(b)), it would be a best practice to use the same classes for both. When an entity does not use the same classes (e.g., in providing disclosures about fair value by level in the fair value hierarchy and quantitative disclosures about significant unobservable inputs), the entity should provide a reconciliation so that the relationship between the classes is clear.

<table>
<thead>
<tr>
<th>Asset</th>
<th>Fair Value (000s)</th>
<th>Valuation Technique(s)</th>
<th>Unobservable Input(s)</th>
<th>Low</th>
<th>High</th>
<th>Weighted Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>RMBS — prime</td>
<td>$ 7,000</td>
<td>Discounted cash flow</td>
<td>Constant prepayment rate</td>
<td>0.00%</td>
<td>8.30%</td>
<td>2.30%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Loss severity</td>
<td>50.00%</td>
<td>70.00%</td>
<td>55.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Constant default rate</td>
<td>0.00%</td>
<td>18.00%</td>
<td>10.00%</td>
</tr>
<tr>
<td>RMBS — subprime</td>
<td>$ 2,000</td>
<td>Discounted cash flow</td>
<td>Constant prepayment rate</td>
<td>0.00%</td>
<td>10.00%</td>
<td>1.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Loss severity</td>
<td>60.00%</td>
<td>100.00%</td>
<td>80.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Constant default rate</td>
<td>0.00%</td>
<td>29.00%</td>
<td>18.00%</td>
</tr>
</tbody>
</table>
11.3.3.1.2 Derivative Contracts

ASC 815-10-50 requires entities to provide tabular disclosures about derivatives by “type of contract.” Depending on the facts and circumstances, the classes of derivative contracts under the ASC 820 fair value disclosure requirements may differ from the type of contracts used to provide tabular disclosures under ASC 815. The classes of derivative contracts may be more disaggregated under ASC 820 than the type of contract under ASC 815 but generally should not be more condensed.

An entity should consider the types of derivative contracts it holds. Under ASC 820-10-50-2B, class is based on the derivatives’ characteristics, nature, risks, and classification in the fair value hierarchy. Class is often at a greater level of disaggregation than the line items in the statement of financial position. Therefore, in determining the characteristics, nature, and risks of its derivative contracts, an entity should consider the following factors (in addition to the type of contracts):

- The valuation techniques and inputs used to determine fair value.
- The valuation processes used to determine fair value.
- The classification in the fair value hierarchy.
- The level of disaggregation in the statement of financial position.

An entity may also consider the level of disaggregation it uses for other ASC 815 disclosures (e.g., qualitative and volume), which may vary from the level of disaggregation it uses for the ASC 815 tabular disclosures.

ASC 320-10-50-1B provides guidance on class determination and useful considerations related to assessing nature and risks for debt securities. On the basis of those requirements, concentrations are likely to be important in the determination of class for all assets and liabilities. For example, an entity that engages in material commodity transactions may consider concentrations by commodity type, or an entity with a material foreign exchange portfolio may consider concentrations by discrete currencies.

11.3.3.1.3 Disposal Group or Assets to Be Disposed Of

An entity may have a long-lived asset disposal group classified as held for sale under ASC 360 (which may include or represent a discontinued operation). The individual assets and liabilities within a disposal group that are measured at fair value on a recurring or nonrecurring basis are subject to the disclosure requirements in ASC 820.

When considering the appropriate classes of assets and liabilities under ASC 820-10-50-2B and preparing fair value disclosures, an entity should distinguish assets and liabilities that are part of a disposal group classified as held for sale from its other assets and liabilities. This separate presentation is consistent with the requirements in ASC 205-20-45-10 and 45-11 and ASC 360-10-45-14, under which an entity must separately disclose the major classes of assets and liabilities of the discontinued operation (or the major classes of assets and liabilities classified as held for sale) either on the face of the statement of financial position or in the notes to the financial statements. The ASC 820 disclosures required for certain items within a disposal group should be consistent with the disclosures under ASC 205-20-45-10 and 45-11 or ASC 360-10-45-14.

19 The assets and liabilities of an asset group to be held and used in an entity’s business would also be subject to ASC 820’s disclosure requirements if they are measured at fair value on a recurring or nonrecurring basis.
Chapter 11 — Disclosure

ASC 360-10-35-43 requires an entity to measure a disposal group at the lower of its carrying amount or fair value less costs to sell. Furthermore, ASC 360-10-35-40 states:

A loss shall be recognized for any initial or subsequent write-down to fair value less cost to sell. A gain shall be recognized for any subsequent increase in fair value less cost to sell, but not in excess of the cumulative loss previously recognized (for a write-down to fair value less cost to sell). The loss or gain shall adjust only the carrying amount of a long-lived asset, whether classified as held for sale individually or as part of a disposal group.

ASC 820-10-50-2(a) requires an entity to disclose, “for recurring fair value measurements, the fair value measurement at the end of the reporting period, and for nonrecurring fair value measurements, the fair value measurement at the relevant measurement date and the reasons for the measurement.” ASC 820-10-55-100 includes an example of a nonrecurring disclosure.

In certain circumstances, an impairment loss may be recognized for some assets within a disposal group that also includes assets and liabilities measured at fair value on a recurring basis. Thus, the asset group contains assets that are measured on both a recurring and nonrecurring basis. In periods in which an impairment of a disposal group is recognized, the nonrecurring fair value disclosures related to that impairment should reflect the incremental amount beyond what has already been disclosed in the recurring and nonrecurring fair value tables for the other assets and liabilities that are included in the disposal group.20 See Example 11-15 below.

Example 11-15

Disposal Group for Which There Are Recurring and Nonrecurring Fair Value Measurements

In November 20X9, Entity B, a calendar-year-end company, enters into an agreement to sell Subsidiary X. The transaction is expected to close in May 20X1. In accordance with ASC 360-10-45-9, X is a disposal group that B presents as held for sale in its December 31, 20X9, balance sheet.

Assume the following:

- The disposal group consists of PP&E and equity securities (real estate industry) measured at fair value through earnings. Subsidiary X does not have intangible assets, goodwill, or liabilities.
- The PP&E has a carrying value of $30 million.
- The fair value of the equity securities (real estate industry) is $65 million, measured on the basis of a quoted price in an active market (Level 1).
- The fair value of the disposal group is $80 million, measured on the basis of significant unobservable inputs (Level 3).
- The cost of selling the disposal group is $10 million.

Therefore, on B’s balance sheet, the disposal group is shown as consisting of $70 million of assets held for sale ($80 million fair value less $10 million costs to sell). The disclosures required by ASC 820-10-50-2(a) and 50-2(b) could be presented in the manner described below.

20 The same approach would apply to long-lived assets held and used that constitute an asset group.
### Example 11-15 (continued)

For the assets measured at fair value on a recurring basis during the period, B would present the following:

<table>
<thead>
<tr>
<th>Fair Value Measurements Using</th>
</tr>
</thead>
<tbody>
<tr>
<td>Description</td>
</tr>
<tr>
<td>Fair Value Amounts (in millions)</td>
</tr>
<tr>
<td>Quoted Prices in Active Markets for Identical Assets (Level 1)</td>
</tr>
<tr>
<td>Year Ended 12/31/X9</td>
</tr>
<tr>
<td>Assets Held for Sale</td>
</tr>
<tr>
<td>Equity securities</td>
</tr>
<tr>
<td>Equity securities — real estate industry</td>
</tr>
<tr>
<td>Total</td>
</tr>
</tbody>
</table>

For the assets measured at fair value on a nonrecurring basis during the period, in addition to narrative disclosures about why this remeasurement was made, B would present the following:

<table>
<thead>
<tr>
<th>Fair Value Measurements Using</th>
</tr>
</thead>
<tbody>
<tr>
<td>Description</td>
</tr>
<tr>
<td>Fair Value Amounts (in millions)</td>
</tr>
<tr>
<td>Quoted Prices in Active Markets for Identical Assets (Level 1)</td>
</tr>
<tr>
<td>Year Ended 12/31/X9</td>
</tr>
<tr>
<td>Disposal group*</td>
</tr>
<tr>
<td>Total</td>
</tr>
</tbody>
</table>

* The total fair value measurement of the disposal group is $80 million, which includes $65 million of equity securities (real estate industry) included in the disclosures regarding assets and liabilities that are measured at fair value on a recurring basis. The remaining fair value for the disposal group is $15 million.

In calculating the fair value amounts for the above disclosure, X considers the guidance in ASC 360 on impairment or disposal of long-lived assets. Subsidiary X (i.e., the disposal group) has a carrying amount of $95 million (PP&E of $30 million and equity securities (real estate industry) of $65 million) and a fair value of $80 million (which includes $65 million of equity securities in real estate). When considering the costs to sell of $10 million, X recognizes an impairment loss of $25 million in earnings for the period (i.e., $80 million fair value, less $95 million carrying cost, less selling costs of $10 million). This loss is recorded as a write-down of the carrying amount of the long-lived assets within the disposal group.

Note that the above presentations represent one alternative; entities should determine that the disclosure objectives in ASC 205-20, ASC 360, and ASC 820, as appropriate, are met for an asset group or disposal group. The entity would also be subject to (1) the disclosure requirements in both ASC 205-20-50 and ASC 360-10-50 and (2) other relevant fair value disclosure requirements in ASC 820-10-50-2.
11.3.3.2 Disclosures Related to the Fair Value Hierarchy

11.3.3.2.1 General

ASC 820-10-50-2(b) requires all entities to disclose the level of the fair value hierarchy within which all recurring and nonrecurring fair value measurements are categorized.21 ASC 820-10-50-2E and ASC 825-10-50-10 also require public business entities to disclose the level of the fair value hierarchy for assets and liabilities that are not measured at fair value but for which fair value is disclosed. Such classifications in the fair value hierarchy are made on the basis of the classification of the asset or liability in its entirety.

Fair value measurements often consist of multiple inputs that span multiple levels within the fair value hierarchy. In these circumstances, the asset or liability is classified in its entirety on the basis of the lowest-level input that is deemed significant to the fair value measurement. See Section 8.1.2 for more information.

11.3.3.2.2 Transfers Between Levels

ASC 820-10-50-2C requires all entities to develop, disclose, and consistently apply a “policy for determining when transfers between levels of the fair value hierarchy are deemed to have occurred.” However, ASC 820 does not prescribe a method for determining the timing of transfers between levels. Rather, ASC 820-10-50-2C indicates that to determine when transfers have occurred, entities may use the fair value of the asset, liability, or instrument classified in a reporting entity’s shareholders’ equity as of (1) “the date of the event or change in circumstances that caused the transfer,” (2) the “beginning of the reporting period,” or (3) the “end of the reporting period,” provided that the approach applied is used consistently. Accordingly, it is not appropriate for an entity to determine the amount of “transfers in” by using the beginning-of-period fair value and the amount of “transfers out” by using the end-of-period fair value, or vice versa. Such an approach is not acceptable because no gain or loss would be attributed to items transferred into or out of Level 3, thus diminishing the usefulness of the Level 3 rollforward disclosure.

Before the adoption of ASU 2018-13, ASC 820-10-50-2(bb) requires other-than-nonpublic entities to disclose, “[f]or assets and liabilities held at the end of the reporting period that are measured at fair value on a recurring basis, the amounts of any transfers between Level 1 and Level 2 of the fair value hierarchy [and] the reasons for those transfers.” Further, the disclosure of transfers into each level must be separate from that for transfers out of each level. However, ASC 820-10-50-2F indicates that nonpublic entities do not need to provide such disclosures unless another Codification topic requires them to do so. All entities are required to disclose (1) their accounting policy “for determining when transfers . . . are deemed to have occurred” (see ASC 820-10-50-2C) and (2) “[t]he amounts of any

21 Assets measured on a recurring basis by using the NAV practical expedient are not subject to such disclosure. See Section 11.3.2.3 for more information.
transfers into or out of Level 3 of the fair value hierarchy and the reasons for those transfers.” Entities would disclose transfers into Level 3 separately from transfers out of Level 3 (see ASC 820-10-50-2(c)(3)).

**Connecting the Dots**

An entity commonly measures the fair value of its assets and liabilities more frequently (e.g., monthly) for internal management reporting purposes than for external reporting purposes. As part of its periodic fair value measurement processes, the entity may incorporate a system for identifying the date of the transfers between levels. The fair value amount for transfers determined through the entity's periodic (i.e., monthly) process could then be used to furnish the disclosures required by ASC 820-10-50-2(bb) and ASC 820-10-50-2(c)(3) at the end of the reporting period.

Example 11-16 illustrates how an entity may determine the date of transfers into or out of Level 3.

### Example 11-16

**Transfers Into or Out of Level 3 of the Fair Value Hierarchy**

Assume the following:

- Entity C holds two securities and is preparing its quarterly financial statements for the period ended September 30, 20X0.
- Security A, which is classified in Level 2 at the beginning of the period (July 1, 20X0), is transferred into Level 3 on July 15, 20X0.
- Security B, which is classified in Level 3 at the beginning of the period (July 1, 20X0), is transferred out of Level 3 (into Level 2) on August 15, 20X0.

The following table illustrates the fair values under the three acceptable methods for disclosing the relevant transfers into and out of Level 3 in accordance with ASC 820-10-50-2C:

<table>
<thead>
<tr>
<th>Security</th>
<th>Method 1 Actual Date of Transfer Fair Value*</th>
<th>Method 2 Beginning of the Reporting Period Fair Value (July 1, 20X0)</th>
<th>Method 3 End of the Reporting Period Fair Value (September 30, 20X0)</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>125 (July 15, 20X0)</td>
<td>150</td>
<td>50</td>
</tr>
<tr>
<td>B</td>
<td>250 (August 15, 20X0)</td>
<td>150</td>
<td>300</td>
</tr>
</tbody>
</table>

* Identifies the date on which transfers in and/or out are deemed to occur on the basis of specific events.
### Example 11-16 (continued)

#### Analysis

<table>
<thead>
<tr>
<th>Impact on Levels</th>
<th>Method 1 Actual Date of Transfer Fair Value</th>
<th>Method 2 Beginning of the Reporting Period Fair Value</th>
<th>Method 3 End of the Reporting Period Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Security A</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Level 2 transfer-out value</td>
<td>(125)</td>
<td>(150)</td>
<td>(50)</td>
</tr>
<tr>
<td>Level 3 transfer-in value</td>
<td>125</td>
<td>150</td>
<td>50</td>
</tr>
<tr>
<td>Gain (loss) reflected in Level 3 rollforward</td>
<td>(75)</td>
<td>(100)</td>
<td>—</td>
</tr>
<tr>
<td><strong>Security B</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Level 2 transfer-in value</td>
<td>250</td>
<td>150</td>
<td>300</td>
</tr>
<tr>
<td>Level 3 transfer-out value</td>
<td>(250)</td>
<td>(150)</td>
<td>(300)</td>
</tr>
<tr>
<td>Gain (loss) reflected in Level 3 rollforward</td>
<td>100</td>
<td>—</td>
<td>150</td>
</tr>
</tbody>
</table>

11.3.3.2.3 Cash Collateral Receivables and Payables

See Section 11.3.3.5.2.3.5 for discussion of the presentation of cash collateral receivables and payables on derivative instruments.

11.3.3.2.4 Assets and Liabilities of a CFE

Under ASC 810, an entity that consolidates an eligible CFE may elect to measure the less observable of the fair value of the CFE’s financial assets or the fair value of the CFE’s financial liabilities by using the more observable of the two measurements. See Section A.19 for information about the additional disclosures an entity is required to provide when it makes this election. See Section 8.1.2 for discussion of the determination of the level of the fair value hierarchy in which an entity should categorize the less observable fair value measurement.

11.3.3.3 Reconciliation of Disclosures to the Statement of Financial Position

11.3.3.3.1 General

Under ASC 820, entities must reconcile the disclosed fair value amounts to the statement of financial position when:

- The classes of assets or liabilities are more disaggregated than the line items in the statement of financial position (see Section 11.3.3.1).
- The amount of an asset or liability on the date of the statement of financial position does not equal the amount of a nonrecurring fair value measurement that was recognized for the asset or liability during the financial reporting period (see Section 11.3.3.3.2).
- An entity estimates the fair value of certain investments by using NAV per share as a practical expedient (see Section 11.3.3.3.3).
11.3.3.3.2 Nonrecurring Fair Value Measurements

ASC 820-10-50-2(a) requires entities to disclose, for nonrecurring fair value measurements, the fair value as of the measurement date and the reasons for the measurement. ASC 820-10-50-2(b) further requires disclosure of the level of the nonrecurring fair value measurement within the fair value hierarchy, which is also determined as of the measurement date. If a nonrecurring fair value measurement occurs on any date other than the date of an entity’s statement of financial position, the entity must, as stated in ASC 820-10-50-2(a), “clearly indicate that the fair value information presented is not as of the period’s end as well as the date or period that the measurement was taken.” In meeting this objective, entities should consider the guidance in ASC 820-10-50-2B, which states, in part, that “[a] reporting entity shall provide information sufficient to permit reconciliation to the line items presented in the statement of financial position.” Thus, the entity should provide supplemental information that reconciles (1) the ASC 820 nonrecurring fair value amounts disclosed and (2) the carrying amount as of the date of the statement of financial position.

For example, assume that a long-lived asset classified as held and used is impaired from its current carrying value of $100 to its fair value of $75 as of November 30, 20X7 (assume a calendar-year-end entity). In this case, the amount disclosed as a nonrecurring fair value measurement will be $75. However, since the asset is held and used, subsequent amortization through December 31, 20X7 (the balance sheet date), is recognized. Assume that $1 of subsequent amortization is recognized in December 20X7. The balance sheet will reflect the amortization, while the nonrecurring disclosure will not. The entity should provide supplemental information that reconciles the ASC 820 nonrecurring amount disclosed to the recorded amount as of the balance sheet date.

In addition, the amount of a nonrecurring fair value measurement may not equal the recognized amount of the asset or liability subject to such measurement on the date the measurement is recognized. For example, ASC 360-10-35-43 requires that a disposal group classified as held for sale be measured at the lower of its carrying amount or fair value less costs to sell. However, ASC 820 clarifies that costs to sell (transaction costs) are not included in a fair value measurement. Thus, when an impairment of a long-lived asset classified as held for sale has occurred during a financial reporting period, the nonrecurring fair value amount disclosed under ASC 820 will not be consistent with the carrying amount reflected in the balance sheet as of the reporting date. As previously stated, entities should provide supplemental information that reconciles the ASC 820 nonrecurring amount disclosed to the recorded amount as of the balance sheet date. See Notes (c)–(e) of Example 9 in ASC 820-10-55-100 for an illustration of such disclosure.

11.3.3.3.3 Certain Entities That Calculate NAV per Share (or Its Equivalent)

As discussed in Section 11.3.2.3, although investments that an entity records when using the practical expedient in ASC 820-10-35-59 are not categorized within the fair value hierarchy, an entity is still required under ASC 820-10-35-54B to provide the amounts that it measured by using the practical expedient so that the fair value of investments included in the fair value hierarchy can be reconciled to the line items presented in the statement of financial position in accordance with ASC 820-10-50-2B. ASC 820-10-50-6A further requires that entities “disclose [additional] information that helps users of its financial statements to understand the nature and risks of the investments.” See Note (f) of Example 9 in ASC 820-10-55-100 for an illustration of such disclosure.

11.3.3.4 Disclosure of Valuation Techniques and Inputs

ASC 820-10-50-2(bbb)(1) requires entities to disclose (1) a description of the valuation technique(s) and inputs for each class of assets and liabilities measured at fair value on a recurring or nonrecurring basis and classified within Level 2 or Level 3 of the fair value hierarchy and (2) any changes in a valuation
approach, a valuation technique, or both in connection with such measurements, as well as the reasons for such changes. In accordance with ASC 820-10-50-7, a change in the valuation approach or valuation technique does not cause an entity to be subject to the disclosure requirements in ASC 250 related to a change in accounting estimate.

The objective of these disclosure requirements is to help financial statement users understand not only the valuation techniques and inputs but also the judgments the entity uses when measuring fair value. To meet this objective, entities should consider disclosing the following information about the valuation techniques and inputs used in Level 2 and Level 3 fair value measurements:

- Whether the entity can choose between various valuation techniques and how it makes that choice.
- A description of the valuation techniques selected and the risks or shortcomings (if any) of those techniques.
- When a model is used, a description of the model and related inputs, as well as how the inputs are sourced.
- If the valuation technique has changed since previous reporting periods, the reason why the entity made the change and a quantification of the change's impact on the financial statements.
- The methods the entity uses to calibrate models to market prices and how frequently it uses those methods.
- A description of the use of broker quotes or pricing services. Such a description may include:
  - How many quotes were obtained, how these quotes were verified, and which brokers or pricing services the entity used and why.
  - A summary of known valuation techniques used by brokers and pricing services and to what extent observable market information, as opposed to unobservable market information, was used to determine the quote.
  - Whether quotes are adjusted and how the ultimate fair value was determined.
  - Whether a quote is binding or nonbinding.
- When an entity measures fair value by using prices for similar instruments, how the entity adjusts these prices to reflect the characteristics of the instruments subject to the measurement.
- The key drivers of value for each significant Level 2 and Level 3 asset/liability class and the extent to which the inputs used are observable or unobservable.
- An entity's consideration of illiquidity when performing the valuation. Factors to consider include:
  - Specific assumptions used.
  - How the assumptions were developed.
  - How and why assumptions changed from period to period.
  - Whether valuation techniques/models changed as a result of the lack of liquidity.
  - Whether alternative valuation techniques for illiquid instruments would have resulted in materially different fair values.
- How the entity's and counterparty's nonperformance risk was taken into consideration in the valuation (e.g., for derivatives or debt instruments).
ASC 820-10-55-103 and 55-104 provide examples illustrating how an entity might comply with the requirement to disclose the valuation techniques and inputs used in the measurement of fair value.

For Level 3 fair value measurements, entities are also required to disclose quantitative information about the significant unobservable inputs used in the measurement (see ASC 820-10-50-2(bbb)(2)) and a description of the valuation processes used by the entity for recurring and nonrecurring fair value measurements (see ASC 820-10-50-2(f)). For recurring fair value measurements, other-than-nonpublic entities must also provide a narrative description of the sensitivity of the fair value measurement with respect to the use of significant unobservable inputs (see ASC 820-10-50-2(g)). Entities are permitted, but not required, to disclose quantitative information about inputs used in Level 1 or Level 2 fair value measurements (i.e., the information that must be disclosed about Level 2 fair value measurements in ASC 820-10-50-2(bbb)(1) may be qualitative instead of quantitative). See Sections 11.3.3.5.1 and 11.3.3.5.5 for more information about the disclosures of unobservable inputs related to Level 3 fair value measurements.

11.3.3.5 Level 3 Measurements

11.3.3.5.1 Quantitative Information About Significant Unobservable Inputs
ASC 820-10-50-2(bbb)(2) requires entities to disclose, for each class of assets and liabilities measured at fair value in the statement of financial position after initial recognition, “quantitative information about the significant unobservable inputs used” in those Level 3 fair value measurements. All entities are exempt from disclosing quantitative information about inputs used in Level 1 and Level 2 fair value measurements; however, entities are permitted to provide disclosures for those measurements when they are similar to the quantitative disclosures of significant inputs required for Level 3 fair value measurements.

In a manner consistent with the FASB’s stated objectives in requiring the aforementioned disclosures, entities must determine the following in providing the Level 3 disclosures required for significant unobservable inputs:

- The types of quantitative information to disclose (see Section 11.3.3.5.1.1).
- How detailed the disclosures should be (i.e., the level of aggregation or disaggregation) (see Section 11.3.3.5.1.2).
- What information should be provided, if any, when the entity uses prices from prior transactions or third-party pricing information (see Section 11.3.3.5.1.3).

11.3.3.5.1.1 Types of Quantitative Information
Entities must use judgment in deciding what types of quantitative information to provide about significant unobservable inputs. ASC 820-10-55-103 includes a sample tabular disclosure suggesting that a reporting entity “might disclose” a range and weighted-average amount to comply with ASC 820-10-50-2(bbb)(2). When an entity’s disclosure concerns just one asset or liability, a range and weighted average are not relevant. In such cases, the entity would provide a single value, the amount actually used

22 See footnotes (e) and (f) of Table 11-4 for exceptions to this disclosure requirement.
23 Paragraph BC38 of ASU 2011-04 states, in part:
The Boards noted that the objective of the disclosure is not to enable users of financial statements to replicate the reporting entity’s pricing models but to provide enough information for users to assess whether the reporting entity’s views about individual inputs differed from their own and, if so, to decide how to incorporate the reporting entity’s fair value measurement in their decisions. The Boards concluded that the information required by the disclosure will facilitate comparison of the inputs used over time, providing users with information about changes in management’s views about particular unobservable inputs and about changes in the market for the assets and liabilities within a particular class. In addition, that disclosure might facilitate comparison between reporting entities with similar assets and liabilities categorized within Level 3 of the fair value hierarchy.
for the significant unobservable input. Thus, a range and weighted average are not required, and such information is not always applicable.

However, management should consider whether the information it plans to provide would enable a reasonable investor (or another financial statement user, such as a regulator) to assess the reporting entity’s views on individual inputs. If, for example, the entity provides a wide range of values but not a weighted average, financial statement users may not be able to understand and evaluate the quantitative information disclosed. A weighted average (or other supplemental information) is often necessary to convey an approximation of the input value used for a significant portion of the items in a given class. Entities may consider narrative disclosures, other types of quantitative information (e.g., mean, median, standard deviation, weighted average if not provided), and other alternatives for appropriately conveying the nature and significance of inputs used.

Making similar observations at the 2012 AICPA Conference on Current SEC and PCAOB Developments, Mark Shannon, associate chief accountant in the SEC’s Division of Corporation Finance, noted that the SEC staff will often request entities to disclose a weighted average of the inputs used in a Level 3 measurement when a registrant has used a wide range of inputs. He suggested that when a weighted average is not meaningful, reporting entities can provide qualitative disclosures about the distribution of the range of values presented. Ideally, this disclosure would address each significant input and describe the reason for the wide range.

Although a range and weighted average are not always required, ASC 820-10-55-104 states that “a reporting entity should provide additional information that will help users of its financial statements to evaluate the quantitative information disclosed.” For example, ASC 820-10-55-104(a) lists the following information that an entity might consider disclosing for RMBSs:

1. The types of underlying loans (for example, prime loans or subprime loans)
2. Collateral
3. Guarantees or other credit enhancements
4. Seniority level of the tranches of securities
5. The year of issue
6. The weighted-average coupon rate of the underlying loans and the securities
7. The weighted-average maturity of the underlying loans and the securities
8. The geographical concentration of the underlying loans
9. Information about the credit ratings of the securities.

Further, ASC 820-10-55-104(b) indicates that for all assets and liabilities, entities should consider disclosing “[h]ow third-party information such as broker quotes, pricing services, net asset values, and relevant market data was taken into account when measuring fair value.” In doing so, entities should consider clearly identifying the fair value of assets and liabilities measured by using third-party information.

11.3.3.5.1.2 Disaggregation of Inputs

Entities must disclose quantitative information about all significant unobservable inputs. The meaning of the term “significant” in this context is the same as that in ASC 820-10-35-37A, which states, in part:

[A] fair value measurement is categorized in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement. Assessing the significance of a particular input to the entire measurement requires judgment, taking into account factors specific to the asset or liability.
ASC 820 does not establish a bright line for significance or mandate that significance be determined quantitatively or be based on any specific quantitative approach. ASC 820-10-35-37A notes that an entity must use judgment in determining significance, “taking into account factors specific to the asset or liability.” Entities should establish a method for determining whether an input is significant to a fair value measurement in its entirety and should apply it consistently. As discussed in Section 8.1.2, one possible method for determining whether an input is significant to a fair value measurement is to use a threshold or percentage of the overall measurement amount as a benchmark for significance. In determining significance when using a particularly complex valuation technique, an entity may need to consider how a particular input or inputs behave within a reasonable range of expected outcomes (i.e., by performing a sensitivity analysis).

While the process described in Section 8.1.2 is generally used to identify only the lowest-level input that is significant to the measurement in its entirety, the same process can be used to identify all significant unobservable inputs. The following is a summary of the process discussed in Section 8.1.2, modified to highlight considerations uniquely relevant to ASC 820-10-50-2(bbb)(2):

1. Determine a threshold or percentage of the overall measurement amount as a benchmark for significance. An entity may determine the threshold by considering whether a reasonable investor would believe that variations in underlying inputs and the resultant variations in fair value measurements would significantly alter the total mix of information available. In making this determination, entities may consider SEC SAB Topic 1.M and PCAOB Auditing Standard 11. “Significance” is not the same as “materiality,” but entities can apply similar concepts to this determination.

2. Inventory all inputs used in a Level 3 fair value measurement (i.e., make a list and ensure that it is complete).

3. Perform a sensitivity analysis for each unobservable input by recalculating fair value, altering the unobservable input so that fair value is calculated by using the low and high values in a range of reasonably possible alternative values for that input. In identifying a range of reasonably possible alternative values, entities could consider (1) prevailing market conditions, (2) input from internal or external specialists, or (3) known or implied amounts in sales or transfer transactions observed for similar assets or liabilities.

4. Determine whether the percentage change in fair value resulting from the sensitivity analysis in step 3 exceeds the benchmark for significance identified in step 1.

5. Because SEC and PCAOB guidance on materiality clearly notes that materiality is not solely a quantitative concept, supplement the quantitative analysis in step 4 with a consideration of qualitative factors such as the nature of the input (e.g., for certain derivatives, all inputs may be considered significant).

6. If the input is determined to be significant on the basis of the above steps, include the input in the tabular fair value disclosure.

7. Repeat these steps for other unobservable inputs identified in step 2.

8. Aggregate individually insignificant inputs by level to determine whether a combination of such inputs is significant to the measurement in its entirety. If so, disclose these inputs.

This process would not need to be repeated in each reporting period unless facts and circumstances change. In identifying significant inputs, management may also consider (1) specialists’ input; (2) competitors’ disclosures, analyst reports, or both; and (3) its own judgment based on experience with the products.

As noted in Section 8.1.2, an entity should not use a percentage of a particular component of a fair value measurement or the income statement effect of a fair value measurement (i.e., the threshold should be based on a balance sheet approach).
11.3.3.5.1.3 Third-Party Pricing Information

Paragraph BC90 of ASU 2011-04 states the following regarding quantitative disclosures about significant unobservable inputs related to use of third-party pricing information:

[T]he Boards understand that fair value is sometimes measured on the basis of prices in prior transactions (for example, adjustments to the last round of financing for a venture capital investment) or third-party pricing information (for example, broker quotes). Such measurements might be categorized within Level 3 of the fair value hierarchy. In such cases, the Boards concluded that the reporting entity should be required to disclose how it has measured the fair value of the asset or liability, but that it should not need to create quantitative information (for example, an implied market multiple or future cash flows) to comply with the disclosure requirement if quantitative information other than the prior transaction price or third-party pricing information is not used when measuring fair value. However, the Boards concluded that when using a prior transaction price or third-party pricing information a reporting entity cannot ignore other quantitative information that is reasonably available. If there was an adjustment to the price in a prior transaction or third-party pricing information that is significant to the fair value measurement in its entirety, that adjustment would be an unobservable input about which the reporting entity would disclose quantitative information, even if the reporting entity does not disclose the unobservable information used when pricing the prior transaction or developing the third-party pricing information.

In considering the guidance in paragraph BC90 of ASU 2011-04, an entity must disclose the following information about its Level 3 fair value measurements:

- How it has used third-party pricing information to measure the fair value of assets or liabilities.
- Quantitative information about significant unobservable inputs used to develop significant adjustments, if any, that the entity applies to third-party pricing information (or prior transactions).
- Quantitative information about significant unobservable inputs used by the third party if such information is reasonably available to the entity.

Entities should make a reasonable effort to gather sufficient qualitative and quantitative information to determine whether fair value measurements based on third-party information are prepared in accordance with ASC 820 and to prepare applicable disclosures about fair value measurements. If, despite an entity's efforts, quantitative information about significant unobservable inputs used by third-party pricing services is not reasonably available, the entity would not be required to create such information. Specifically, ASC 820-10-50-2(bbb)(2) states, in part:

A reporting entity is not required to create quantitative information to comply with this disclosure requirement if quantitative unobservable inputs are not developed by the reporting entity when measuring fair value (for example, when a reporting entity uses prices from prior transactions or third-party pricing information without adjustment). However, when providing this disclosure, a reporting entity cannot ignore quantitative unobservable inputs that are significant to the fair value measurement and are reasonably available to the reporting entity.

Notwithstanding this guidance, management must understand the information furnished by third-party service providers. If third-party service providers supply entities with details about the methods and assumptions used and with quantitative information to support the entity's efforts to comply with the disclosure requirements in ASC 820, quantitative information about significant unobservable inputs may be reasonably available and should be disclosed.
Quantitative information about significant unobservable inputs used by a third party may become reasonably available to the entity in various ways, including, but not limited to:

- Recalculation of substantially all fair value measurements provided by third parties for a given class of asset or liability as part of the reporting entity's process to ensure that these measurements are developed in accordance with ASC 820 or to comply with management's responsibilities outlined in ASC 820-10-35-54K through 35-54M.\(^{25}\)

- Inquiry and examination of supplemental information provided by third parties to (1) comply with management's responsibilities or (2) support a leveling disclosure (ASC 820-10-50-2(b)) and other required disclosures.

- ASC 820 does not clearly address whether an other-than-nonpublic entity is subject to the requirement in ASC 820-10-50-2(g) to disclose qualitative information about the sensitivity of a Level 3 fair value measurement that results from the use of unobservable inputs when the entity does not disclose quantitative information about significant unobservable inputs used by a third-party pricing service to develop the fair value measurement. In the absence of further clarification from standard setters or regulatory bodies, an entity should make a reasonable effort to disclose useful qualitative information about the sensitivity of a Level 3 fair value measurement that results from the use of unobservable inputs. Such information might be obtained as part of management's process for understanding the valuation techniques and assumptions that the third party used in measuring fair value. See Section 10.8 for more information about management's responsibilities when it uses fair value information provided by a third party.

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\(^{25}\) Note that entities are generally not required to disclose quantitative inputs about techniques that are used to validate other valuation techniques (e.g., secondary techniques that are not weighted in the fair value measurement). However, a description of the validating procedure would be relevant information about an entity's valuation processes that it should consider disclosing in accordance with ASC 820-10-50-2(f) and ASC 820-10-55-105. See also Section 11.3.3.5.4.
11.3.3.5.1.4 Examples

ASC 820-10-55-103 and 55-104 illustrate the disclosure of quantitative information about significant unobservable inputs. Below is an additional example.

Example 11-17

Disclosure of Quantitative Information About Significant Unobservable Inputs

Entity D invests in various equity securities and RMBSs. In accordance with ASC 820-10-50-2B, D identifies three classes of equity securities, differentiating each class on the basis of the investees’ industry, and three classes of RMBSs based on the creditworthiness of underlying mortgage holders. (Note that an entity is not required to differentiate classes of debt investments on the basis of creditworthiness but should consider disaggregating classes when nature, characteristics, or risks differ in accordance with ASC 820-10-50-2B.) The following table presents the fair value by level within the fair value hierarchy for corresponding measurements as of December 31, 20X2:

<table>
<thead>
<tr>
<th>Description</th>
<th>Fair Value (000s)</th>
<th>Level 1</th>
<th>Level 2</th>
<th>Level 3</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity securities</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity securities — real estate industry</td>
<td>$ 93,000</td>
<td>$ 70,000</td>
<td>$ 23,000</td>
<td></td>
</tr>
<tr>
<td>Equity securities — oil and gas industry</td>
<td>45,000</td>
<td>45,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity securities — other</td>
<td>15,000</td>
<td>15,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total equity securities</td>
<td>$ 153,000</td>
<td>$ 130,000</td>
<td>$ 23,000</td>
<td></td>
</tr>
<tr>
<td>Available-for-sale debt securities</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>RMBSs</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>RMBS — agency</td>
<td>36,000</td>
<td>24,000</td>
<td>12,000</td>
<td></td>
</tr>
<tr>
<td>RMBS — prime</td>
<td>7,000</td>
<td>7,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>RMBS — subprime</td>
<td>6,000</td>
<td>6,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Commercial mortgage-backed securities</td>
<td>50,000</td>
<td></td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Total available-for-sale debt securities</td>
<td>99,000</td>
<td></td>
<td>74,000</td>
<td>25,000</td>
</tr>
<tr>
<td>Total recurring fair value measurements</td>
<td>$ 252,000</td>
<td>$ 130,000</td>
<td>$ 97,000</td>
<td>$ 25,000</td>
</tr>
</tbody>
</table>

For the $25 million of Level 3 RMBSs, D uses unadjusted third-party information to measure the $16 million fair value of the RMBSs as follows: (1) $12 million of agency-backed RMBSs and (2) $4 million (of the $6 million) of subprime RMBSs. In preparing its fair value disclosures, D makes reasonable efforts to gather qualitative and quantitative information about the methods and assumptions used by third parties to price these RMBSs. Entity D concludes that it has sufficient information to comply with all other disclosure requirements but is not able to gather sufficient quantitative information about significant unobservable inputs used by third parties in their fair value measurements. Entity D has qualified for the disclosure exception in ASC 820-10-50-2(bbb)(2). Paragraph BC90 of ASU 2011-04 provides additional information on this issue.
Example 11-17 (continued)

Entity D prepares the following disclosure of quantitative information about significant unobservable inputs:

**Example A — Potentially Insufficient Disclosure**

<table>
<thead>
<tr>
<th>Asset</th>
<th>Fair Value (000s)</th>
<th>Valuation Technique(s)</th>
<th>Unobservable Input(s)</th>
<th>Low</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>RMBSs</td>
<td>$9,000</td>
<td>Discounted cash flow</td>
<td>Discount rate</td>
<td>4.25%</td>
<td>17.89%</td>
</tr>
</tbody>
</table>

This disclosure may be confusing to financial statement users because it is not reconciled to D’s disclosure of fair value measurements by level in the fair value hierarchy. That is, the $9 million in RMBSs shown above is only a portion of the RMBSs held by the entity (the $7 million in prime RMBSs and $2 million (of the $6 million) in subprime RMBSs) and it is unclear from this disclosure whether the quantitative information is related to agency, prime, or subprime RMBSs. In addition, the remaining $16 million of RMBSs for which fair value measurements are based on unadjusted third-party information should be disclosed. Paragraph BC90 of ASU 2011-04 states that for such cases, “the Boards concluded that the reporting entity should be required to disclose how it has measured the fair value of the asset.”

**Example B — Potentially Insufficient Disclosure**

<table>
<thead>
<tr>
<th>Asset</th>
<th>Fair Value (000s)</th>
<th>Valuation Technique(s)</th>
<th>Unobservable Input(s)</th>
<th>Low</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>RMBSs</td>
<td>$25,000</td>
<td>Discounted cash flow</td>
<td>Discount rate</td>
<td>4.25%</td>
<td>17.89%</td>
</tr>
<tr>
<td></td>
<td>Vendor pricing</td>
<td>Price</td>
<td></td>
<td>$50.00</td>
<td>$115.00</td>
</tr>
</tbody>
</table>

This presentation may also be confusing to financial statement users because it is not clear whether (1) two different techniques were used to measure different portions of the $25 million in RMBSs or (2) both techniques were used to develop a range of estimates. An entity that develops a range of estimates must evaluate the reasonableness of the range and choose a point within the range that is most representative of fair value. In such cases, other unobservable inputs might include (1) the weight applied to each technique or (2) a valuation adjustment.

In addition, when all RMBSs are aggregated into one class, users may not be able to understand how the nature and risks differ for assets within the class. See Section 11.3.3.1 for a discussion of identifying classes of assets and liabilities in disclosures about fair value measurements. Entities are not always required to disaggregate RMBSs into the classes identified in this example. Section 11.3.3.1 further discusses the use of differing classes of assets or liabilities in fair value disclosures that ASC 820-10-50-2 requires for each class of asset or liability.

Further, a range of amounts used for each unobservable input, though helpful, may not tell the full story. Users might assume that there is more uncertainty in the inputs than actually exists.

Moreover, an entity often uses multiple assumptions (i.e., underlying inputs) to develop discount rates, particularly when performing a discounted cash flow fair value measurement for RMBSs, debt instruments, derivatives, and other financial assets. If, after performing the process to identify significant inputs described in Section 11.3.3.5.1.2, the entity considers underlying inputs individually significant to the entire measurement, the entity should separately disclose such inputs. Assume that D performs the procedures described in Section 11.3.3.5.1.2 for identifying significant unobservable inputs and concludes that the discount rate consists of the following:

- Level 2 risk-free interest rate based on U.S. Treasury yields.
- Level 3 assumptions about prepayment speeds.
- Level 3 assumptions about loss severities.
- Level 3 assumptions about default rates.
Example 11-17 (continued)

The following example illustrates how D might disclose information about these inputs and how it might address the issues identified above:

**Example C — More Robust Disclosure**

<table>
<thead>
<tr>
<th>Asset</th>
<th>Fair Value (000s)</th>
<th>Valuation Technique(s)</th>
<th>Unobservable Input(s)</th>
<th>Low</th>
<th>High</th>
<th>Weighted Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>RMBS — agency</td>
<td>$ 12,000</td>
<td>Vendor pricing</td>
<td>Price</td>
<td>$ 102.00</td>
<td>$ 115.00</td>
<td>$ 104.00</td>
</tr>
<tr>
<td>RMBS — prime</td>
<td>$ 7,000</td>
<td>Discounted cash flow</td>
<td>Constant prepayment rate</td>
<td>0.00%</td>
<td>8.30%</td>
<td>2.30%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Loss severity</td>
<td>50.00%</td>
<td>70.00%</td>
<td>55.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Constant default rate</td>
<td>0.00%</td>
<td>18.00%</td>
<td>10.00%</td>
</tr>
<tr>
<td>RMBS — subprime</td>
<td>$ 2,000</td>
<td>Discounted cash flow</td>
<td>Constant prepayment rate</td>
<td>0.00%</td>
<td>10.00%</td>
<td>1.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Loss severity</td>
<td>60.00%</td>
<td>100.00%</td>
<td>80.00%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Constant default rate</td>
<td>0.00%</td>
<td>29.00%</td>
<td>18.00%</td>
</tr>
<tr>
<td>RMBS — subprime</td>
<td>$ 4,000</td>
<td>Vendor pricing</td>
<td>Price</td>
<td>$ 50.00</td>
<td>$ 65.00</td>
<td>$ 58.00</td>
</tr>
</tbody>
</table>

This presentation alternative results in more relevant information for financial statement users than the approaches in the previous examples, enabling them to better understand and evaluate the techniques and inputs used. The benefits of this presentation alternative include:

- Disclosing the fair value for measurements derived by using a given technique when multiple techniques were used makes it clear what technique was used to measure the fair value for respective portions of D's RMBSs.
- Disaggregating the asset class gives users insight into the different assumptions used when risk and other characteristics differ.
- Disaggregating the discount rate into individually significant inputs increases the transparency of the assumptions used by management and the sources of potential uncertainty in the fair value measurements.
- Disclosing a weighted-average value for each input helps users understand the values applied to a majority of the securities in a given class.

11.3.3.5.2 Level 3 Fair Value Rollforward

11.3.3.5.2.1 General

As discussed in Section 11.3.2.1, ASC 820-10-50-2(c) requires all entities to disclose a “reconciliation from the opening balances to the closing balances” (i.e., beginning-of-period to end-of-period balances) for all classes of assets and liabilities measured at fair value on a recurring basis that are classified within Level 3 of the fair value hierarchy. In that reconciliation, the following must be disclosed in tabular format:

- “Total gains or losses for the period recognized in earnings” by income statement line item.
- “Total gains or losses for the period recognized” in OCI by line items in the statement of other comprehensive income.
- “Purchases, sales, issues, and settlements” (each of which is separately disclosed).
- The amount of transfers “into or out of Level 3 of the fair value hierarchy” and the reasons for those transfers (with transfers into Level 3 disclosed and discussed separately from transfers out of Level 3).
The example in ASC 820-10-55-101 illustrates how an entity might comply with this requirement.

### 11.3.3.5.2.2 Day 1 Gains or Losses

When the transaction price differs from the exit price at initial recognition of an asset or liability that is recognized at fair value on a recurring basis, an inception (or “day 1”) gain or loss is recognized in earnings. The impact of day 1 gains and losses should be included in the Level 3 rollforward disclosure as well as in the disclosure required by ASC 820-10-50-2(d). A separate line item identifying the impact of day 1 gains or losses is not required unless an entity reports a “dealer profit” (i.e., day 1 gain) in an income statement line item separate from other gains and losses on derivatives. See Example 11-18 for a related illustration. Also see Section 9.2 for further discussion of when the transaction price differs from the exit price at initial recognition of an asset or liability.

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**Example 11-18**

**Impact of Day 1 Gain on Level 3 Rollforward**

Entity E, a broker-dealer, enters into a long-dated derivative contract with a counterparty in which it pays the counterparty $5 million at execution of the trade. However, E determines that it has not transacted in the principal (or most advantageous) market for the long-dated derivative (i.e., E can exit the long-dated derivative in the interdealer market at a higher price). Entity E determines that the fair value at inception is $8 million and that the inputs to the valuation of the long-dated derivative have a significant impact as a result of Level 3 inputs. At the end of the reporting period, E determines that the fair value of the long-dated derivative is $12 million (still with significant effects from Level 3 inputs). Entity E would provide the following disclosure regarding the long-dated derivative at the end of the period (in millions):

**Beginning Balance**

<table>
<thead>
<tr>
<th></th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total gains or losses (realized and unrealized):</td>
<td></td>
</tr>
<tr>
<td>(a) Recognized in earnings (included in other gain/loss*)</td>
<td>7</td>
</tr>
<tr>
<td>(b) Recognized in other comprehensive income (included in derivative gain/loss*)</td>
<td>—</td>
</tr>
<tr>
<td>Purchases</td>
<td>5</td>
</tr>
<tr>
<td>Sales</td>
<td>—</td>
</tr>
<tr>
<td>Issues</td>
<td>—</td>
</tr>
<tr>
<td>Settlements</td>
<td>—</td>
</tr>
<tr>
<td>Transfers into Level 3**</td>
<td>—</td>
</tr>
<tr>
<td>Transfers out of Level 3**</td>
<td>—</td>
</tr>
</tbody>
</table>

**Ending Balance**

<table>
<thead>
<tr>
<th></th>
<th>$ 12</th>
</tr>
</thead>
</table>

The amount of total gains or losses for the period recognized in earnings attributable to the change in unrealized gains or losses relating to assets still held at the end of the reporting period (included in other gain/loss*)

<table>
<thead>
<tr>
<th></th>
<th>$ 7</th>
</tr>
</thead>
</table>

* A reporting entity is required to identify the line item in the statement of income or in the statement of comprehensive income (if applicable) in which the change in value, resulting from the fair value measurement, was recorded.

** A reporting entity is required to discuss the reasons for the transfers into and out of Level 3 and its policy for determining when such transfers have occurred.

Under ASC 820, E would not be required to separately identify the day 1 gain or loss (i.e., the $3 million profit at inception calculated as the difference between the $8 million fair value at inception and the $5 million transaction price) in the rollforward or supplemental disclosures unless it reports a “dealer profit” (i.e., day 1 gain) in a separate income statement line item. In either case, in the period of the transaction, the day 1 gain or loss is a component of the rollforward.
11.3.3.5.2.3 Derivatives

11.3.3.5.2.3.1 General

In preparing the Level 3 rollforward, an entity needs to take additional considerations into account for classes of assets and liabilities that meet the definition of a derivative instrument under ASC 815. Those considerations are explained below.

11.3.3.5.2.3.2 Determination of Gains and Losses on Financial and Physical Derivatives

ASC 820-10-50-2(c)(1) requires all entities to disclose “total gains or losses for the period recognized in earnings . . . and the line item(s) in the statement of income . . . in which those gains or losses are recognized," and ASC 820-10-50-2(c)(1a) requires all entities to disclose “total gains or losses for the period recognized in other comprehensive income, and the line item(s) in other comprehensive income in which those gains or losses are recognized." Further, ASC 815-10-50-4A through 50-4F require entities to provide separate disclosures about the location and amount of all gains and losses reported in the income statement for derivatives. Specifically, ASC 815-10-50-4A(b) requires the following disclosures:

The location and amount of the gains and losses on derivative instruments (and such nonderivative instruments) and related hedged items reported in any of the following:
1. The statement of financial performance
2. The statement of financial position (for example, gains and losses initially recognized in other comprehensive income).

The objectives of the gain and loss disclosure requirements of ASC 820 and ASC 815 are to provide information about the performance of an entity’s derivative instruments from an economic perspective (i.e., the impact of derivative instruments on the equity of the entity through net earnings or OCI).26 Neither the disclosure requirement in ASC 820-10-50-2(c)(1)/(c)(1a) nor that in ASC 815-10-50-4A(b) distinguishes between financially and physically settled derivatives (i.e., those that are settled gross through the receipt or delivery of the underlying asset in exchange for cash). The objectives of the gain and loss disclosure requirements for derivative instruments in ASC 820 are the same as those in ASC 815, regardless of whether the instruments are financially or physically settled. Moreover, although the scope of ASC 820-10-50-2(c)(1)/(c)(1a) is broader than that of ASC 815-10-50 in one respect (i.e., it applies to all recurring fair value measurements, not just derivative instruments) and narrower in another respect (i.e., it applies only to Level 3 measurements), the method an entity uses to determine the amount of gains or losses to disclose under ASC 820-10-50-2(c)(1)/(c)(1a) should be consistent with the method it uses to determine the amount of gains or losses under ASC 815-10-50-4A(b). ASC 815-10-50 implicitly suggests that the amount of gains and losses to be disclosed includes both realized and unrealized gains and losses, which is consistent with the disclosure requirement in ASC 820-10-50-2(c)(1)/(c)(1a).

For financial derivatives, economic performance is demonstrated by the changes in fair value and resulting net settlements that occur over the life of the instrument. The determination of gains or losses on financial derivatives is based on the cash settlement activity. In contrast, physical fixed-price derivatives feature a gross exchange of an underlying asset (e.g., a physical commodity) and cash based on a pre-established price. However, the objective of the gain or loss disclosure remains the same — that is, to require entities to provide information about the performance of the derivative instrument from an economic perspective.

26 Paragraphs 82 and 83 of FASB Concepts Statement 6 define gains (or losses) as increases (or decreases) in “equity (net assets) from peripheral or incidental transactions of an entity and from all other transactions and other events and circumstances affecting the entity except those that result from revenues [or expenses] or investments by [or distributions to] owners.” Further, paragraph 87 states, “[r]evenues and expenses are commonly displayed as gross inflows or outflows of net assets, while gains and losses are usually displayed as net inflows or outflows.”
For example, a physical fixed-price forward commodity contract economically consists of two elements:27

1. A physical purchase or sale of the underlying commodity at the market price on the date of delivery. This results in a physical receipt or delivery of the commodity at its spot market price at the time of the settlement of the contract.

2. A financial fixed-price forward contract based on the same underlying commodity as the physical purchase or sale. This results in a hypothetical net cash settlement based on the difference between the spot market price of the commodity at the time of the settlement of the contract and the fixed price established by the physical derivative contract.

The second element’s change in fair value during the reporting period (i.e., the financial fixed-price forward contract) should be reflected as a gain or loss in the required disclosures. This approach achieves symmetry between financial and physical derivatives and provides financial statement users with relevant information about derivative performance.

Reflecting gross settlement amounts for physical derivatives in the settlement line of the ASC 820 Level 3 rollforward (i.e., the full settlement amount, including cash flows from the physical market purchase or sale element) would constitute an overstatement of gains or losses and would fail to reflect the economic impact of the contract on an entity’s equity. For example, a physical sale that is accounted for as a derivative instrument, that does not contain a financing element (e.g., that does not contain off-market terms or necessitate an up-front cash payment), and that is settled at the money (i.e., the spot market price equals the fixed price at the time of the settlement of the contract) does not result in any net economic benefit or detriment. An entity that enters any amount other than zero in the settlement line of the ASC 820 Level 3 rollforward would be required to increase or decrease another line of the reconciliation (presumably gain or loss) to balance the reconciliation. However, reflecting the gross sales price established by the contract as a derivative gain would be a misrepresentation because it would ignore the fact that the entity delivered an asset of equal value. Likewise, a physical purchase that is accounted for as a derivative, that does not contain a financing element, and that is settled at the money does not result in an economic detriment, and reflecting the gross purchase price established by the contract as a derivative loss would be misrepresentative because the entity received an asset of equal value.

Example 11-19 illustrates the application of this guidance to financial derivatives and physical derivatives. In contemplating how gains or losses are determined and ultimately disclosed, an entity should also consider the guidance in ASC 820-10-50-2B and assess the appropriate classes of assets and liabilities for disclosure.

### Example 11-19

<table>
<thead>
<tr>
<th>Financial Contract</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
<tr>
<td><strong>Financial Derivative 1</strong></td>
</tr>
<tr>
<td>Beginning balance</td>
</tr>
<tr>
<td>Change in fair value</td>
</tr>
<tr>
<td>Cash received</td>
</tr>
<tr>
<td>Ending balance</td>
</tr>
</tbody>
</table>

---

27 For simplicity, physical delivery risk (sometimes referred to as “index” risk), which is typically considered in the fair value calculation of a physical derivative, is not discussed here.
### Example 11-19 (continued)

#### Level 3 Rollforward

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning balance</td>
<td>$ 100</td>
</tr>
<tr>
<td>Total gains or losses recognized in earnings (realized and unrealized)</td>
<td>260*</td>
</tr>
<tr>
<td>Transfers into Level 3</td>
<td>—</td>
</tr>
<tr>
<td>Transfers out of Level 3</td>
<td>—</td>
</tr>
<tr>
<td>Purchases</td>
<td>—</td>
</tr>
<tr>
<td>Sales</td>
<td>—</td>
</tr>
<tr>
<td>Issues</td>
<td>—</td>
</tr>
<tr>
<td>Settlements</td>
<td>(110)**</td>
</tr>
<tr>
<td>Ending balance</td>
<td>$ 250</td>
</tr>
</tbody>
</table>

* Represents change in fair value of derivative 1 ($10) and change in fair value of derivative 2 ($250).
** Represents cash received on settlement.

#### Physical Contract

<table>
<thead>
<tr>
<th>Description</th>
<th>Physical Derivative 1</th>
<th>Physical Derivative 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Description</td>
<td>(Sale of 100 MMBtu of Natural Gas at $8 per MMBtu)</td>
<td>(Sale of 100 MMBtu of Natural Gas at $12 per MMBtu)</td>
</tr>
<tr>
<td>Beginning balance</td>
<td>$ 100</td>
<td>N/A — Entered into during period</td>
</tr>
<tr>
<td>Change in fair value</td>
<td>10</td>
<td>$ 250</td>
</tr>
<tr>
<td>Cash received</td>
<td>800</td>
<td>N/A</td>
</tr>
<tr>
<td>Market value of commodity delivered</td>
<td>690</td>
<td>N/A</td>
</tr>
<tr>
<td>Ending balance</td>
<td>—</td>
<td>$ 250</td>
</tr>
</tbody>
</table>

#### Level 3 Rollforward

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning balance</td>
<td>$ 100</td>
</tr>
<tr>
<td>Total gains or losses recognized in earnings (realized and unrealized)</td>
<td>260*</td>
</tr>
<tr>
<td>Transfers into Level 3</td>
<td>—</td>
</tr>
<tr>
<td>Transfers out of Level 3</td>
<td>—</td>
</tr>
<tr>
<td>Purchases</td>
<td>—</td>
</tr>
<tr>
<td>Sales</td>
<td>—</td>
</tr>
<tr>
<td>Issues</td>
<td>—</td>
</tr>
<tr>
<td>Settlements</td>
<td>(110)**</td>
</tr>
<tr>
<td>Ending balance</td>
<td>$ 250</td>
</tr>
</tbody>
</table>

* Represents change in fair value of derivative 1 ($10) and change in fair value of derivative 2 ($250).
** Represents cash received on settlement.

* Represents change in fair value of derivative 1 ($10) and change in fair value of derivative 2 ($250).
** Represents settlement of the financial fixed-price forward component of the physical derivative. The fixed price is the cash received on gross settlement ($800) that is offset against the spot market price for gas (underlying the physical derivative) at settlement. In this illustration, the spot price is assumed to be $6.90 per MMBtu or $690.
See Section 11.3.3.5.2.3.3 for discussion of how to determine the amounts of purchases, sales, issues, and settlements of derivative instruments that entities must reflect in the Level 3 rollforward.

11.3.3.5.2.3.3 Determination of Purchases, Sales, Issues, and Settlements for Derivatives

ASC 820-10-50-2(c)(2) requires all entities to disclose “purchases, sales, issues, and settlements (each of those types of changes disclosed separately)” as part of the Level 3 rollforward. When determining the amounts to disclose for individual derivative contracts for purchases, sales, issues, and settlements, an entity should evaluate the consideration exchanged (e.g., cash) between the counterparty and itself. However, an entity should not offset cash collateral receivables and payables with derivative assets and liabilities (see Section 11.3.3.5.2.3.5).

Typically, a derivative transaction that does not involve an up-front exchange of consideration (e.g., an at-market swap) should not be disclosed in the purchases, sales, or issues line items. Any ongoing payments under the contract would be reflected in the settlements line item. An up-front payment may not be required for an option acquired by an entity; instead, the entity may be required to make periodic premium payments to the counterparty over the term of the contract (i.e., the option premium is effectively financed by the counterparty). In this situation, the entity should consider the deferred premium payments as ongoing settlements rather than an up-front exchange of consideration, which the entity would typically present in the purchases line item.

The guidance below outlines the presentation of various types of payments related to derivative contracts within the Level 3 rollforward as purchases, sales, issues, or settlements.

- **Purchases** — An entity should present a derivative requiring an initial cash outlay (or other up-front consideration) in the purchases line item. Such presentation would include premium payments to purchase an option or up-front payments related to an off-market swap asset. Payments to acquire a derivative asset (through a contract assignment) should also be presented in the purchases line item.

- **Sales** — If an entity assigns a derivative asset to a third party for consideration, the payment should be presented in the sales line item. An assignment of a derivative liability should be disclosed as a settlement rather than as a sale (see the discussion in the “Settlements” bullet below for further details).

- **Issues** — If an entity executes a derivative and receives an initial cash inflow (or other up-front consideration), the up-front payment should be presented in the issues line item. In this situation, the entity has issued a derivative liability in return for consideration. Such presentation would include receipt of premium payments on written options or receipt of up-front payments related to an off-market swap liability. Payments received to assume a derivative contract liability (through a contract assignment) should also be presented in the issues line item and accompanied by separate disclosure describing the nature of the assignment transaction and the assignment amount related to the transaction. Alternatively, an entity may adopt a policy of presenting the consideration related to assignments of derivative liabilities in a separate line item other than purchases, sales, issues, or settlements, along with a disclosure describing the nature of the assignment transactions.

- **Settlements** — All ongoing contractual cash payments (or other consideration) made under the derivative contract should be disclosed in the settlements line item. Such disclosure would include payments on a multiperiod settled derivative (e.g., interest rate swaps that are net-cash-settled on a quarterly basis) or payments between the entity and counterparty to terminate a derivative or to exercise an option. In addition, if an entity assigns a derivative liability to a third party and is required to make a payment to the third party as part of the transaction,
the payment should be presented in the settlements line item and accompanied by separate disclosure describing the nature of the assignment transaction and the settlement amount related to the transaction. An assignment of a derivative liability is akin to an early termination and thus a settlement of the original derivative. Alternatively, an entity may present the consideration related to assignments of derivative liabilities in a separate line item other than purchases, sales, issues, or settlements, along with a disclosure describing the nature of the assignment transactions.

Table 11-5 summarizes the application of ASC 820-10-50-2(c)(2) to various derivative transactions and highlights the concept of symmetry between the entity and counterparty.

<table>
<thead>
<tr>
<th>Transaction (From Reporting Entity's Perspective)</th>
<th>Presentation by:</th>
<th>Reporting Entity</th>
<th>Counterparty (or Third-Party Assignee)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchase of an option for up-front premium</td>
<td></td>
<td>Purchases</td>
<td>Issues</td>
</tr>
<tr>
<td>Writing of an option for up-front premium</td>
<td></td>
<td>Issues</td>
<td>Purchases</td>
</tr>
<tr>
<td>Assignment of derivative asset contract to a third party (assignee makes payment)</td>
<td></td>
<td>Sales</td>
<td>Purchases</td>
</tr>
<tr>
<td>Assignment of derivative liability contract to a third party (assignee receives payment)</td>
<td></td>
<td>Settlements*</td>
<td>Issues*</td>
</tr>
<tr>
<td>Periodic cash settlement of a swap contract</td>
<td></td>
<td>Settlements</td>
<td>Settlements</td>
</tr>
<tr>
<td>Early termination of derivative contract between parties to original contract</td>
<td></td>
<td>Settlements</td>
<td>Settlements</td>
</tr>
</tbody>
</table>

* If an entity adopts a policy of disclosing the consideration related to assignments of derivative liabilities as settlements (for assignments to third parties) or issues (for assignments from third parties), the entity should also include a separate disclosure describing the nature of the assignment transactions and the settlement amounts related to the transactions. Alternatively, an entity may adopt a policy of presenting the consideration related to assignments of derivative liabilities in a separate line item other than purchases, sales, issues, or settlements, along with a disclosure describing the nature of the assignment transactions. This policy should be disclosed and consistently applied.

Example 11-20 illustrates the application of this guidance to financial derivative instruments.

**Example 11-20**

**Determination of Purchases, Sales, Issues, and Settlements for Financial Derivative Instruments**

Assume the following:

- **Financial Derivative 1** — Beginning balance of $100 asset; $10 change in fair value during period (i.e., increase in the fair value of the asset); termination cash payment of $110; zero ending balance.

- **Financial Derivative 2** — Beginning balance of $0; entity wrote a strip of interest rate caps and received consideration of $100; $500 change in fair value of derivative during period (i.e., increase in the fair value of the liability); one cap was exercised by the counterparty, for which a cash outflow of $75 during the period was required; ending derivative liability of $525.

- **Financial Derivative 3** — Beginning balance of $0; entity purchased an option for $50 up front; $30 change in fair value during period (decrease in the fair value of the asset); no settlement or exercise during the period; ending derivative asset of $20.

The entity has determined that Financial Derivative 1, Financial Derivative 2, and Financial Derivative 3 are separate classes (separate rollforwards are therefore required). See Section 11.3.3.1.2 for guidance on determining classes of derivative contracts.
### Example 11-20 (continued)

#### Level 3 Rollforward in Period 1*

<table>
<thead>
<tr>
<th>Financial Derivative 1</th>
<th>Financial Derivative 2</th>
<th>Financial Derivative 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning balance</td>
<td>$100</td>
<td>—</td>
</tr>
<tr>
<td>Total gains or (losses)</td>
<td>10</td>
<td>(500)</td>
</tr>
<tr>
<td>Transfers</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Issues</td>
<td></td>
<td>(100)</td>
</tr>
<tr>
<td>Settlements</td>
<td>(110)</td>
<td>75</td>
</tr>
<tr>
<td>Ending balance</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* Negative balances in the sales, issues, and settlements line items of this example represent cash inflows. The reconciliation is required to be presented not on a derivative-by-derivative basis but by class of derivative contract.

Assume the following additional facts (related to preparation of the disclosures for the second reporting period):

- **Financial Derivative 1** — Settled in prior period.
- **Financial Derivative 2** — Beginning liability balance of $525; $80 change in fair value of derivative during period (decrease in the fair value of the liability); no regular settlements during the period.
- **Financial Derivative 3** — Beginning asset balance of $20; $5 change in fair value during period (decrease in the fair value of the asset); no settlement or exercise during the period.

Upon downgrade of its credit rating by a rating agency, the entity is forced to terminate its entire portfolio of derivatives. The entity makes one cash payment of $430 to assign **Financial Derivative 2** and **Financial Derivative 3** to an independent third party.

#### Level 3 Rollforward in Period 2*

<table>
<thead>
<tr>
<th>Financial Derivative 2</th>
<th>Financial Derivative 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning balance</td>
<td>$ (525)</td>
</tr>
<tr>
<td>Total gains or (losses)</td>
<td>80</td>
</tr>
<tr>
<td>Transfers</td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td></td>
</tr>
<tr>
<td>Issues</td>
<td></td>
</tr>
<tr>
<td>Settlements**</td>
<td>445</td>
</tr>
<tr>
<td>Ending balance</td>
<td></td>
</tr>
</tbody>
</table>

* Negative balances in the sales, issues, and settlements line items of this example represent cash inflows. The reconciliation is required to be presented not on a derivative-by-derivative basis but by class of derivative contract.

** The entity's accounting policy is to present the consideration paid to assign its derivative liabilities to third parties as settlements. The entity would also include a separate disclosure describing the nature of the assignment transaction and the settlement amount related to the transaction.
11.3.3.5.2.3.4 Gross Versus Net Presentation of Purchases, Sales, Issues, and Settlements for Derivatives

In accordance with ASC 820-10-50-2(c)(2), all entities must present, as part of the Level 3 rollforward, purchases, sales, issues, and settlements related to derivative instruments. ASC 820-10-50-3(b) addresses whether derivative assets and derivative liabilities must be presented on a gross or net basis in the Level 3 rollforward and allows entities to present derivative instruments on either a gross or net basis. Whether an entity chooses to present derivative instruments net (i.e., in one table) or gross (i.e., derivative assets and liabilities in two separate tables), the entity must still present purchases, sales, issues, and settlements separately for each class of derivative contract. That is, an entity that chooses to present derivative instruments on a net basis under ASC 820-10-50-3(b) is still required to separate the purchases, sales, issues, and settlements related to those derivatives by class in complying with the Level 3 rollforward requirement in ASC 820-10-50-2(c)(2). See also Examples 11-21 and 11-22 below.

Example 11-21

**Entity Purchases an Option and Writes an Option**

Assume the following:

- Entity F has a policy of presenting derivative contracts on a net basis in accordance with ASC 820-10-50-3(b).
- Entity F acquires an option for a $50 up-front payment and separately writes an option in return for a $100 up-front payment during the same period.
- In aggregating the fair value disclosures, F determines the class to be the same for each option.

It would not be appropriate for F to net the $50 purchase with the $100 issue and present a net $50 issue. Rather, F should, in the Level 3 rollforward, separately present the $50 purchase and $100 issue that occurred during the period.

Further assume that in a subsequent period, offsetting cash payments are made on these options. In this situation, because both option contracts are considered to be in the same class for aggregation purposes, F should net the subsequent payments associated with these contracts and present the net amount in the “settlements” line item.

Example 11-22

**Entity Assigns Derivative Asset and Derivative Liability**

Assume the following:

- Entity G chooses to present derivative contracts on a net basis in accordance with ASC 820-10-50-3(b).
- Entity G has a derivative asset with a fair value of $100 and a derivative liability with a fair value of $25.
- In aggregating the fair value disclosures, G determines the class to be the same for each derivative.
- During the period, G assigns the derivative asset and derivative liability to an independent third party in return for a cash payment of $75.

In this scenario, it would be acceptable for G to present the $75 payment received in the “sales” line item. Alternatively, G could allocate the $75 payment between the derivative asset and derivative liability and present these amounts separately in the Level 3 rollforward; the $100 related to the derivative asset would be presented in the sales line item and the $25 related to the derivative liability would be presented in the settlements line item. Entity G could also present the derivative liability portion in a separate line item within the rollforward (e.g., a line item called “assignments of liabilities”). See Section 11.3.3.5.2.3.3 for additional guidance on presenting various types of payments related to derivative contracts within the Level 3 rollforward as purchases, sales, issues, or settlements. Regardless of the policy it selects, G should also include a separate disclosure describing the nature of the assignment transaction and the settlement amounts related to the transaction.

If G were instead to make a net payment to the third party in this example to assign a net derivative liability, G should present such a payment as a settlement. An allocation between the settlement of a derivative liability and sale of a derivative asset would also be acceptable.
11.3.3.5.2.3.5 Presentation of Cash Collateral Receivables and Payables

Under ASC 815-10-45-3 through 45-7, an entity may elect to offset, in its statement of financial position, fair value amounts recognized for its derivative instruments with fair value amounts recognized for the right or obligation to reclaim or return cash collateral (i.e., offset its derivative assets and liabilities with cash collateral receivables and payables). An entity that makes this election should not offset cash collateral receivables and payables with derivative assets and liabilities in ASC 820 disclosures, including the Level 3 rollforward. Although such fair value amounts are offset in the statement of financial position, such offsetting is inappropriate in the ASC 820 disclosures because doing so would be misleading. For example, assume that the net amount is the credit exposure under a particular master netting arrangement rather than the fair value amounts (measurements) of the derivative positions. Disclosure of the net amount would not allow financial statement users to identify the fair value amounts of the derivative instruments and where they are categorized in the fair value hierarchy. Example 11-23 illustrates an acceptable way of presenting the cash collateral receivables and payables in the ASC 820 disclosures.

Example 11-23

Presentation of Cash Collateral on Derivative Instruments

Cash collateral receivables and payables are presented in a separate column with other counterparty netting adjustments made under ASC 815-10-45-3 through 45-7. The entity uses the separate column to facilitate reconciliation with the balance sheet.

<table>
<thead>
<tr>
<th>Description</th>
<th>Quoted Prices in Active Markets for Identical Assets (Level 1)</th>
<th>Significant Other Observable Inputs (Level 2)</th>
<th>Significant Unobservable Inputs (Level 3)</th>
<th>Counterparty and Cash Collateral Netting</th>
<th>Amount Report in the Balance Sheet as of 12/31/X8</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trading securities</td>
<td>$105</td>
<td>$10</td>
<td>$0</td>
<td>$0</td>
<td>$115</td>
</tr>
<tr>
<td>Derivative assets</td>
<td></td>
<td></td>
<td></td>
<td>(15)*</td>
<td>45</td>
</tr>
<tr>
<td>Total assets</td>
<td>$130</td>
<td>$25</td>
<td>$20</td>
<td>(15)</td>
<td>160</td>
</tr>
<tr>
<td>Derivative liabilities</td>
<td>$45</td>
<td>$65</td>
<td>$10</td>
<td>(35)*</td>
<td>85</td>
</tr>
<tr>
<td>Total liabilities</td>
<td>$45</td>
<td>$65</td>
<td>$10</td>
<td>(35)</td>
<td>85</td>
</tr>
</tbody>
</table>

* Amounts represent the effect of legally enforceable master netting arrangements between the reporting entity and its counterparties and the payable or receivable for cash collateral held or placed with the same counterparties.

Note that this presentation method for cash collateral receivables and payables and other counterparty netting adjustments made under ASC 815-10-45-3 through 45-7 does not apply in other circumstances (e.g., portfolio-level adjustments). See Section 11.3.3.5.6 for guidance on the allocation of portfolio-level adjustments.
11.3.3.5.3 Unrealized Gains and Losses on Level 3 Assets and Liabilities

ASC 820-10-50-2(d) requires all entities to separately disclose, “[f]or recurring fair value measurements categorized within Level 3 of the fair value hierarchy, the amount of the total gains or losses for the period . . . included in earnings . . . that is attributable to the change in unrealized gains or losses relating to those assets and liabilities held at the end of the reporting period, and the line item(s) . . . in which those unrealized gains or losses are recognized.” In determining the unrealized portion of total gains or losses on Level 3 assets or liabilities held at the end of the reporting period, an entity should follow its established and disclosed policy for determining when transfers between levels of the fair value hierarchy are deemed to have occurred (see Section 11.3.3.2.2) to ensure that amounts are reconciled to the amounts presented in the Level 3 rollforward (see Section 11.3.3.5.2). ASC 820-10-55-102 contains an example illustrating how an entity might separately disclose the unrealized portion of total gains and losses, by respective financial statement line item, as required by ASC 820-10-50-2(d).

11.3.3.5.4 Valuation Processes for Level 3 Assets and Liabilities

ASC 820-10-50-2(f) requires all entities to disclose a description of the valuation processes used for all recurring and nonrecurring Level 3 fair value measurements. Paragraph BC91 of ASU 2011-04 indicates that this disclosure requirement was added “because users of financial statements told the Boards that information about a reporting entity's valuation processes helps them to assess the relative subjectivity of the reporting entity's fair value measurements, particularly for those categorized within Level 3 of the fair value hierarchy.” See ASC 820-10-55-105 for related implementation guidance.

11.3.3.5.5 Qualitative Sensitivity Disclosure for Level 3 Assets and Liabilities

ASC 820-10-50-2(g) requires other-than-nonpublic reporting entities to disclose “a narrative description of the sensitivity of [a] fair value measurement to changes in unobservable inputs if a change in those inputs to a different amount might result in a significantly higher or lower fair value measurement.” Entities should consider, at a minimum, the sensitivity to changes in those unobservable inputs disclosed in accordance with ASC 820-10-50-2(bbb) when complying with this disclosure requirement and should also disclose any interrelationships between significant unobservable inputs that might exacerbate those measurement differences. The objective of such disclosure(s) is to help financial statement users understand not only the valuation techniques and inputs but also the judgments the entity uses when measuring fair value. See ASC 820-10-55-106 for further implementation guidance, including a sample disclosure about RMBSs.

In accordance with ASC 820-10-50-2F, nonpublic entities are not required to disclose the information required by ASC 820-10-50-2(g) unless another Codification topic requires them to do so.

11.3.3.5.6 Use of Net Risk Exception for Portfolio-Based Fair Value Measurements

Under ASC 820-10-35-18D, the fair value of a group of financial assets, financial liabilities, nonfinancial items accounted for as derivatives in accordance with ASC 815, or combinations of these items can be measured on the basis of what would be received to exit a net-long or net-short risk position, provided that certain provisions are met. ASC 820-10-50-2D requires an entity to disclose the fact that it made an accounting policy decision to use the exception in ASC 820-10-35-18D. See Section 10.2.8 for further discussion of this valuation approach.

CVAs are commonly made at the portfolio level as long as the requirements outlined in ASC 820-10-35-18E through 35-18H are met. An entity might incorporate the effect of exposure to a particular counterparty's credit by netting its derivative asset and liability contracts with a given counterparty in accordance with a master netting arrangement and then calculate a CVA on the basis of the net position.
with the counterparty. Thus, a CVA might apply to, and be calculated on the basis of, a portfolio of contracts that are individually classified in different levels of the fair value hierarchy. ASC 820-10-35-18L provides the following additional guidance about CVAs:

[The reporting entity shall include the effect of the reporting entity's net exposure to the credit risk of that counterparty or the counterparty's net exposure to the credit risk of the reporting entity in the fair value measurement when market participants would take into account any existing arrangements that mitigate credit risk exposure in the event of default (for example, a master netting agreement with the counterparty or an agreement that requires the exchange of collateral on the basis of each party's net exposure to the credit risk of the other party). The fair value measurement shall reflect market participants' expectations about the likelihood that such an arrangement would be legally enforceable in the event of default.

As long as the requirements outlined in ASC 820-10-35-18E through 35-18H are met, mid-to-bid or mid-to-ask adjustments can also be made at the portfolio level. A derivatives dealer might initially use the midpoint in the bid-ask spread to value a portfolio of both its long (buys) and short (sells) derivative positions with the same underlying. The derivatives dealer would then make a mid-to-bid or mid-to-ask adjustment to effectively move the net open position of the portfolio to the bid or ask depending on whether the portfolio is net long or net short each period. Thus, a mid-to-bid or mid-to-ask adjustment might apply to, and be calculated on the basis of, all of a portfolio's derivative contracts that are individually classified in different levels of the fair value hierarchy. ASC 820-10-35-18I through 35-18K discuss additional considerations related to when an entity that uses the exception in ASC 820-10-35-18D is exposed to market risks and measures fair value.

An entity must allocate portfolio-level adjustments to the individual assets and liabilities in complying with ASC 820's disclosure requirements. ASC 820-10-35-18G indicates the following:

A reporting entity shall make an accounting policy decision to use the exception in paragraph 820-10-35-18D. A reporting entity that uses the exception shall apply that accounting policy, including its policy for allocating bid-ask adjustments (see paragraphs 820-10-35-18I through 35-18K) and credit adjustments (see paragraph 820-10-35-18L), if applicable, consistently from period to period for a particular portfolio.

Emphasis added]

The ASC 820 disclosure requirements must be applied in a manner consistent with the asset's, liability's, or own equity instrument's unit of account (which is generally specified by Codification topics other than ASC 820). This is the case even when the ASC 820-10-35-18D exception has been applied. The unit of account under ASC 815 is each individual derivative. Accordingly, a CVA related to a portfolio of derivatives must be allocated to each individual derivative contract within the portfolio.

ASC 820 does not prescribe an approach for allocating portfolio-level adjustments to individual assets and liabilities. However, ASC 820-10-35-18G requires that an entity's policy be consistently applied. Entities must apply a reasonable method for allocating portfolio-level adjustments and should consider disclosing their policy in the notes to the financial statements.

An allocated portfolio adjustment is an input in the measurement of the fair value of the contract. Accordingly, an allocated portfolio adjustment that is a Level 3 input (i.e., either the portfolio adjustment or the allocation itself is unobservable) and that has a significant effect on the measurement of fair value of an individual asset, liability, or own equity instrument would cause the fair value of the entire individual asset, liability, or own equity instrument to be considered Level 3. Therefore, if a CVA is made on the basis of unobservable inputs, and that amount is allocated to individual derivative instruments within a portfolio, each individual derivative would represent a Level 3 fair value measurement solely on the basis of the CVA allocation if that allocation is significant to the measurement of this individual derivative instrument in its entirety.

28 Because some derivatives can be assets or liabilities depending on changes in market conditions, entities may employ more sophisticated techniques that factor in reasonably possible market fluctuations in determining the appropriate CVA. For simplicity, this guidance assumes that current exposure approximates expected exposure.
11.4 Examples of Financial Instruments Subject to the Disclosure Requirements of ASC 825-10-50-10

The following are examples of financial instruments that are subject to the fair value disclosure requirements of ASC 825-10-50-10 (i.e., financial instruments of public business entities that are not measured at fair value but for which fair value disclosures are required):

- Cash equivalents and short-term investments.
- Investment securities.
- Long-term investments.
- Loan receivables.
- Note receivables.
- Long-term receivables.
- Short-term debt.
- Long-term debt.
- Long-term payables.
- Commitments to extend credit.
- Standby letters of credit.
- Written financial guarantees.
- Foreign currency contracts.
- Tender option bonds.
- Repurchase agreements.
- Reverse repurchase agreements.
- Treasury rolls.
- Mortgage dollar rolls.
- Lines of credit.
- Variable-rate demand preferred shares.
- Variable-rate muni term preferred shares.
Chapter 12 — Fair Value Option

12.1 Introduction

ASC 825-10

05-5 The Fair Value Option Subsections of this Subtopic address both of the following:
   a. Circumstances in which entities may choose, at specified election dates, to measure eligible items at fair value (the fair value option)
   b. Presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities.

05-6 See Topic 820 for guidance on fair value measurements.

10-1 The objective of the guidance in the Fair Value Option Subsections of this Subtopic is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions.

Entities

15-2 The guidance in this Subtopic applies to all entities.

Under ASC 825, entities can elect the FVO to account for certain financial assets and financial liabilities at fair value. The change in fair value of the eligible item that is elected under the FVO is recognized in net income (or, for certain financial liabilities, in net income and OCI as discussed in Section 12.4.1.2).

The FVO may be elected for any eligible item within the scope of ASC 825 (see Section 12.2). The ability to elect the FVO is not predicated on the reliability of the fair value measurement. In ASC 820, the FASB rejected a minimum-reliability threshold for items that are carried at fair value (under the FVO or otherwise). That is, the FASB decided to allow fair value measurements for items in financial statements even when they are not based on market-observable data. In such circumstances, however, the data used for the measurement must reflect assumptions that market participants would use in pricing the asset or liability (including adjustments that market participants demand for the risk associated with the unobservable data or the model used to determine fair value). In addition, entities are required to disclose the categorization of fair value measurements within the fair value hierarchy, which indicates whether significant inputs to those measurements are observable or unobservable.

1 In these circumstances, the entity applies the fair value measurement guidance in ASC 820.
12.2 Scope

12.2.1 General

ASC 825-10

Instruments

15-4 All entities may elect the fair value option for any of the following eligible items:

a. A recognized financial asset and financial liability, except any listed in the following paragraph

b. A firm commitment that would otherwise not be recognized at inception and that involves only financial instruments (for example, a forward purchase contract for a loan that is not readily convertible to cash — that commitment involves only financial instruments — a loan and cash — and would not otherwise be recognized because it is not a derivative instrument)

c. A written loan commitment

d. The rights and obligations under an insurance contract that has both of the following characteristics:
   1. The insurance contract is not a financial instrument (because it requires or permits the insurer to provide goods or services rather than a cash settlement).
   2. The insurance contract's terms permit the insurer to settle by paying a third party to provide those goods or services.

e. The rights and obligations under a warranty that has both of the following characteristics:
   1. The warranty is not a financial instrument (because it requires or permits the warrantor to provide goods or services rather than a cash settlement).
   2. The warranty's terms permit the warrantor to settle by paying a third party to provide those goods or services.

f. A host financial instrument resulting from the separation of an embedded nonfinancial derivative from a nonfinancial hybrid instrument under paragraph 815-15-25-1, subject to the scope exceptions in the following paragraph (for example, an instrument in which the value of the bifurcated embedded derivative is payable in cash, services, or merchandise but the debt host is payable only in cash).

12.2.1.1 Financial Asset or Financial Liability

Generally, all entities may elect the FVO for all financial assets or financial liabilities. However, there are certain exceptions, as discussed in Section 12.2.2.

12.2.1.1.1 Equity Method Investees That Hold Nonfinancial Assets and Nonfinancial Liabilities

An equity method investment meets the definition of a financial asset. An investor is not required to “look through” the investment to the investee's assets and liabilities to determine eligibility for the FVO. The FVO is available for equity method investments regardless of the nature of the investee's assets and liabilities. However, certain nonconsolidated equity investments subject to the equity method may be ineligible for the FVO under ASC 825 because of a significant future-services component, as discussed in Section 12.2.2.6.

12.2.1.2 Written Loan Commitment

An entity should consider the definition of a “loan commitment” in the ASC master glossary when determining whether an item represents a written loan commitment for which the FVO may be elected. Only the writer of a loan commitment can elect the FVO. The FVO is not available to the holder of the loan commitment.
12.2.1.3 Warranty Contracts

An entity should consider the definition of a “warranty” in the ASC master glossary when determining whether an item represents a warranty contract for which the FVO may be elected.

12.2.1.4 Host Financial Instrument

12.2.1.4.1 Hybrid Financial Instrument

A host financial instrument that is recognized separately because an embedded financial derivative in the hybrid financial instrument has been separated under ASC 815-15 is not eligible for the FVO. However, the entire hybrid financial instrument is eligible for the FVO provided that none of the exceptions in ASC 825-10-15-5 apply to the instrument.

12.2.1.4.2 Hybrid Nonfinancial Instrument

A host financial instrument that is recognized separately because an embedded nonfinancial derivative in the hybrid nonfinancial hybrid instrument has been separated under ASC 815-15 is eligible for the FVO under ASC 825-10-15-4(f) provided that none of the exceptions in ASC 825-10-15-5 apply to the instrument. Such eligibility depends on both (1) the bifurcation and separate accounting for the embedded derivative instrument under ASC 815-15 and (2) the determination that what remains after such bifurcation is a financial instrument (i.e., the host contract is a financial instrument). Thus, the FVO is not available for an embedded derivative that is subject to an exception in ASC 815 (i.e., an embedded feature that is not separately accounted for under ASC 815-15).

It is important for an entity to identify the features of the separated embedded derivative and the remaining host contract. If the appropriately identified embedded derivative contains all of the nonfinancial features of the hybrid nonfinancial instrument and the host contract is receivable or payable only in cash, the host contract would be considered a financial asset or liability. If the identified features of the host contract contain any nonfinancial items (e.g., delivery of commodities, services), the host contract is not a financial instrument and the entity may not elect to apply the FVO under ASC 825-10-15-4. An entity must use judgment in determining the features of the embedded derivative and host contract.

12.2.1.4.3 Examples

Example 12-1

Prepaid Forward Commodity Contract — Embedded Derivative Is Not Bifurcated

Entity A enters into a prepaid contract to sell a commodity. The contract must be physically settled, and the commodity is not readily convertible to cash. The contract is a hybrid nonfinancial instrument that does not meet the definition of a derivative instrument in its entirety.

Entity A may not elect the FVO for the contract because (1) the hybrid instrument is not a financial instrument (since the contract must be physically settled by delivering a nonfinancial asset) and (2) the embedded commodity is not separated from the host debt contract under ASC 815-15. If the commodity had met the definition of a derivative and been bifurcated from the host contract, A would have been able to apply the FVO to the host financial instrument. See Example 12-2 for a scenario in which the embedded derivative is bifurcated from the host contract.
Chapter 12 — Fair Value Option

Example 12-2

Prepaid Forward Commodity Contract — Embedded Derivative Is Bifurcated

Entity B enters into a prepaid contract to sell a commodity. Under the contract, B receives $1 million from the counterparty at inception of the contract and will deliver a fixed quantity of the commodity every month for the next 60 months. The contract must be physically settled, and the commodity is readily convertible to cash. The contract is a hybrid nonfinancial instrument that does not meet the definition of a derivative instrument in its entirety.

Entity B determines that the embedded derivative is bifurcated as a commodity forward in which B receives a fixed dollar amount and delivers the fixed quantity of the commodity every month. Entity B will separately account for the bifurcated derivative at fair value in accordance with ASC 815-15-25-1. Entity B identifies the host contract as a payable in which it received $1 million at inception in return for future deliveries of the commodity to the counterparty. Because the identified host contract is a financial asset, B may elect to apply the FVO under ASC 825-10-15-4 to the host contract upon initial recognition (or on another eligible election date).

Example 12-3

Prepaid Services Contract — Embedded Derivative Is Bifurcated

Entity C enters into a contract to buy a fixed dollar amount of services from Entity D every month for 60 months. Entity C will pay an amount each month for six months that comprises a fixed dollar amount multiplied by an index linked to a foreign currency, Y, which is not the functional currency of either party and whose economic characteristics and risks are not clearly and closely related to either party’s services. Entity C identifies the embedded derivative as a net-cash-settled foreign-currency derivative and the host contract as a contract for services. The embedded derivative will be accounted for at fair value in accordance with ASC 815-15-25-1. Because the host contract is not a financial instrument, C may not elect to account for it at fair value under ASC 825-10-15-4.

12.2.2 Exceptions

ASC 825-10

Instruments

15-5 No entity may elect the fair value option for any of the following financial assets and financial liabilities:

a. An investment in a subsidiary that the entity is required to consolidate.

b. An interest in a variable interest entity (VIE) that the entity is required to consolidate.

c. Employers’ and plans’ obligations (or assets representing net overfunded positions) for pension benefits, other postretirement benefits (including health care and life insurance benefits), postemployment benefits, employee stock option and stock purchase plans, and other forms of deferred compensation arrangements, as defined in Topics 420; 710; 712; 715; 718; and 960.

d. Financial assets and financial liabilities recognized under leases as defined in Subtopic 840-10. (This exception does not apply to a guarantee of a third-party lease obligation or a contingent obligation arising from a cancelled lease.)

e. Deposit liabilities, withdrawable on demand, of banks, savings and loan associations, credit unions, and other similar depository institutions.

f. Financial instruments that are, in whole or in part, classified by the issuer as a component of shareholders’ equity (including temporary equity) (for example, a convertible debt instrument within the scope of the Cash Conversion Subsections of Subtopic 470-20 or a convertible debt security with a noncontingent beneficial conversion feature).
No entity may elect the fair value option for any of the following financial assets and financial liabilities:

- An investment in a subsidiary that the entity is required to consolidate.
- An interest in a variable interest entity (VIE) that the entity is required to consolidate.
- Employers’ and plans’ obligations (or assets representing net overfunded positions) for pension benefits, other postretirement benefits (including health care and life insurance benefits), postemployment benefits, employee stock option and stock purchase plans, and other forms of deferred compensation arrangements, as defined in Topics 420; 710; 712; 715; 718; and 960.
- Financial assets and financial liabilities recognized under leases as defined in Subtopic 842-10. (This exception does not apply to a guarantee of a third-party lease obligation or a contingent obligation arising from a cancelled lease.)
- Deposit liabilities, withdrawable on demand, of banks, savings and loan associations, credit unions, and other similar depository institutions.
- Financial instruments that are, in whole or in part, classified by the issuer as a component of shareholders’ equity (including temporary equity) (for example, a convertible debt instrument within the scope of the Cash Conversion Subsections of Subtopic 470-20 or a convertible debt security with a noncontingent beneficial conversion feature).

### 12.2.2.1 Consolidated Entities

An entity cannot elect the FVO to avoid consolidating another entity under the voting or VIE consolidation model in ASC 810. In the Background Information and Basis for Conclusions of Statement 159, the FASB noted that an “interest in an entity (principally an investment in a subsidiary or a primary beneficiary’s variable interest in a variable interest entity) that would otherwise be consolidated” would be outside the scope of the FVO because the FVO “should not be used to make significant changes to consolidation practices.” While an entity cannot elect the FVO for the entire consolidated entity, it is permitted to elect the FVO for underlying financial assets and financial liabilities held by the consolidated entity that are eligible items.

### 12.2.2.2 Employers’ and Plans’ Obligations

As noted in ASC 825-10-15-S(c), entities may not elect the FVO for “[e]mployers’ and plans’ obligations (or assets representing net overfunded positions) for pension benefits, other postretirement benefits (including health care and life insurance benefits), postemployment benefits, employee stock option and stock purchase plans, and other forms of deferred compensation arrangements.” Rather, these items must be recognized in accordance with the relevant guidance in ASC 420, ASC 710, ASC 712, ASC 715, ASC 718, or ASC 960.

### 12.2.2.3 Financial Assets and Financial Liabilities Related to Leases

Financial assets and financial liabilities associated with lease accounting are not eligible for the FVO. Rather, they must be accounted for under ASC 840 or ASC 842, as applicable. However, the FVO may be elected for a guarantee of a third-party lease obligation or a contingent obligation arising from a canceled lease.


12.2.2.4 Deposit Liabilities

Under ASC 825-10-15-5(e), “[d]eposit liabilities, withdrawable on demand, of banks, savings and loan associations, credit unions, and other similar depository institutions” are not eligible for the FVO. Rather, they must be accounted for under ASC 942-405.

12.2.2.5 Financial Instruments Classified in Equity

ASC 825-10-15-5(f) excludes “[f]inancial instruments that are, in whole or in part, classified by the [entity] as a component of shareholders’ equity (including temporary equity)” from the scope of the FVO. Such financial instruments include the following:

- Common stock.
- Equity-classified derivatives indexed to an entity’s common stock.
- Convertible preferred stock.
- Redeemable preferred stock (not mandatorily redeemable).
- Convertible debt within the scope of the cash conversion subsections of ASC 470-20.
- Convertible debt with a beneficial conversion feature that is recognized in equity.
- Convertible debt with a previously bifurcated conversion option that was reclassified to equity.
- Convertible debt issued at a substantial premium that is recognized in equity.
- Convertible debt with a modified conversion feature that is recognized in equity.
- Noncontrolling interest (e.g., common stock, preferred stock, or equity-classified derivatives issued by a consolidated subsidiary).

The above financial instruments would be measured at fair value through earnings only in the unusual circumstance in which the guidance in ASC 815-15-35-2 was applicable (see Section 12.2.3.2.3 for further discussion). Examples 12-4 and 12-5 below illustrate how an entity would consider beneficial conversion features in determining whether convertible debt instruments qualify for the FVO.

Example 12-4

Convertible Debt Instrument — No Beneficial Conversion Feature

Entity D has issued a debt instrument that is convertible by the holder into shares of D's common stock. Before considering whether to elect the FVO for this convertible debt instrument, D must determine whether the instrument would be classified, in whole or in part, within stockholders’ equity. In this example, assume the following:

- There is no beneficial conversion feature under ASC 470-20 that must be recognized as of the issuance date of the convertible debt instrument.
- There is no cash conversion feature within the scope of ASC 470-20.

Since no part of the convertible debt instrument is classified in stockholders’ equity at issuance, D is permitted to elect the FVO for the instrument. ASC 825 does not preclude an entity from electing the FVO for a convertible debt instrument if the conversion option, on a freestanding basis, would have been classified in stockholders’ equity, provided that there is no component of the convertible debt instrument that must be separately classified in stockholders’ equity.
Connecting the Dots

A convertible debt instrument may contain an embedded conversion feature that is beneficial (i.e., “in-the-money”) upon issuance. If that beneficial conversion feature is separately recognized in equity, the FVO is not available. However, if that embedded conversion feature would need to be bifurcated under ASC 815-15, no beneficial conversion feature would be recognized in equity upon issuance (i.e., the beneficial element would constitute a component of the liability that would be recognized for the embedded conversion option); therefore, the FVO could be elected for the entire convertible debt instrument. That is, in accordance with ASC 815-15 and ASC 825, if a convertible debt instrument contains an embedded derivative that must be bifurcated, the entity can avoid such bifurcation by electing to apply a fair value measurement to the convertible debt instrument in its entirety. If the entity decides to bifurcate the embedded derivative in lieu of electing the FVO, the entity cannot apply the FVO to the bifurcated host contract because ASC 825-10-25-11 prohibits an entity from separating a financial instrument that is legally a single contract into parts to apply the FVO. (Because the convertible debt instrument is a financial instrument, ASC 825-10-15-4(f), which permits an entity to elect the FVO for a host financial instrument that remains after an embedded nonfinancial derivative instrument is bifurcated from a nonfinancial hybrid instrument, does not apply.)

Example 12-5

Convertible Debt Instrument — Contingent Beneficial Conversion Feature

Entity E issues a convertible debt instrument that contains a contingent beneficial conversion feature. Because a contingent beneficial conversion feature is not separately recognized within stockholders’ equity upon issuance, a convertible debt instrument with a contingent beneficial conversion feature is eligible for the FVO provided that no other exceptions in ASC 825-10-15-5 are applicable. Thus, E can elect the FVO for the convertible debt instrument.

If, after election of the FVO, the contingency is triggered, the instrument would continue to be subject to fair value measurement, because the FVO (1) may be elected only one time, (2) is irrevocable, and (3) is applied to the entire instrument. In this situation, ASC 825 effectively overrides the guidance on contingent beneficial conversion features in ASC 470-20 once the FVO has been elected.

12.2.2.6 Significant Future-Services Component

Nonconsolidated equity investments that are subject to the equity method of accounting meet the definition of a financial asset because they represent an ownership interest. However, in addition to providing the holder with an equity-like return, such instruments may compensate the investor for significant future services. An example of such a financial instrument is a general partnership interest in which the general partner (GP) has significant management responsibilities (such as managing the partnership’s assets) and is entitled to a return that includes compensation for those future services (e.g., that is disproportionate to the capital invested). Another example is a venture in which (1) an investor will provide future services to the venture and (2) the return from the venture is greater than it would be if the venture paid an unrelated third party for those services.

Because service contracts are not eligible for the FVO under ASC 825, financial instruments with significant service components are also not eligible for the FVO. An entity that applied the FVO to these types of instruments would recognize a day 1 gain (i.e., profit at inception) that represents, in part, compensation for future services. As a result, revenue would be recognized before the performance of related services. This conclusion is consistent with that reached in informal discussions with the SEC and FASB staffs.
An entity should consider all relevant circumstances and exercise judgment when determining whether a financial instrument includes a significant future-services component, particularly when the component is not explicitly stated in the contract terms or the investee's articles of incorporation. The investor's obligation to provide services may be established in a contract different from that of the equity ownership interest, or the service contract may contain only a portion of the economic compensation, with the remainder intended to be an element of the “equity instrument.” Entities should consider the substance of the arrangement and whether the financial instrument and the contract for services are interdependent or inseparable.

The following are some indicators that a significant component of an equity investment consists of compensation for the investor's future services:

- The fair value of the investment includes a return that is disproportionately greater than the return to other passive investors, and the services that the investor provides to the investee affect the future payout under the provision.
- The fair value of the interest at inception is greater than the investor's investment, and the investor is expected to provide services to the investee that are beyond those ordinarily expected of an investor acting solely as a nonmanagement owner.

Because ASC 825-10-25-2 requires an entity to apply the FVO to an entire instrument unless the instrument must be bifurcated under other U.S. GAAP, there is no opportunity for the entity to separate the element for future services and elect the FVO for the portion of the instrument that is purely financial.

Example 12-6

**General Partnership Interest**

Manager A, the only GP of Partnership X, has invested a nominal amount, 1 percent of the total capital, for its general partnership interest. This interest entitles A to 5 percent of X's net income. Manager A does not provide any services to X other than some insignificant administrative tasks; X's assets are managed by an unrelated third party. Manager A receives a disproportionately higher return than the LPs because of its unlimited liability as GP for the partnership's obligations. Manager A estimates the fair value of its general partnership interest to be equal to the amount invested at inception. The general partnership interest does not appear to include significant future services and therefore is eligible for the FVO under ASC 825.

Example 12-7

**General Partnership Interest and Limited Partnership Interest**

Manager B, the GP of Partnership Y, has invested a nominal amount, 1 percent of the total capital, for its general partnership interest. This interest entitles B to 10 percent of Y's net income and provides significant additional compensation if Y's operating margin reaches certain thresholds. Manager B estimates that the fair value of the general partnership interest is greater than the amount invested at inception. Manager B also manages Y's assets through a separate services contract and receives a servicing fee. In addition, there are certain restrictions on the sale of the general partnership interest during the term of the services contract. Moreover, B holds a limited partnership interest in Y that can be transferred independently of the general partnership interest. Manager B invested the same amount as other LPs for its limited partnership interest and receives the same return on its interest as the other LPs. Manager B estimates that the fair value of the limited partnership interest is equal to the amount invested for this instrument. In this example, B could not elect to measure the general partnership interest at fair value under the FVO in ASC 825 because this interest appears to include compensation for significant future services. However, B could elect to measure its limited partnership interest at fair value under the FVO in ASC 825 because this interest does not appear to include significant future services.
Example 12-8

Securitization Entity

Bank C transfers financial assets to a securitization trust in a transfer that is accounted for as a sale. Bank C provides servicing of the financial assets (e.g., collection) for the trust. The servicing contract is initially measured at fair value under ASC 860. (Note that C may elect to subsequently measure a class of servicing assets or servicing liabilities at fair value in accordance with ASC 860-50.) Bank C holds the residual beneficial interest issued by the trust and determines that the fair value of its residual interest is greater than the allocated cost of this retained interest. Bank C also determines that the residual interest meets the definition of a debt security under ASC 320. Bank C could classify its residual interest as a trading security under ASC 320 and measure it at fair value, with changes in fair value recognized in earnings. Because C may classify the security as trading under ASC 320, it would not elect to measure the security at fair value under ASC 825.

12.2.2.6.1 Investments in Affordable Housing Projects

Section 42 of the Internal Revenue Code allows for affordable housing credits. ASC 323-740-05-3 describes these tax credits as follows:

The following discussion refers to and describes a provision within the Revenue Reconciliation Act of 1993; however, it shall not be considered a definitive interpretation of any provision of the Act for any purpose. The Revenue Reconciliation Act of 1993, enacted in August 1993, retroactively extended and made permanent the affordable housing credit. Investors in entities that manage or invest in qualified affordable housing projects receive tax benefits in the form of tax deductions from operating losses and tax credits. The tax credits are allowable on the tax return each year over a 10-year period as a result of renting a sufficient number of units to qualifying tenants and are subject to restrictions on gross rentals paid by those tenants. These credits are subject to recapture over a 15-year period starting with the first year tax credits are earned. Corporate investors generally purchase an interest in a limited liability entity that manages or invests in the qualified affordable housing projects.

An entity that has an ownership interest in an affordable housing entity may elect the FVO for this interest provided that all of the following conditions are met:

• The investment is not consolidated (e.g., it is otherwise subject to the equity method of accounting).

• The ownership interest is a financial asset. Although the FVO is not permitted for current or deferred income tax assets and liabilities because they are not contractual, the amount of tax credits to be received by the investor in a qualified affordable housing project is generally known as part of the partnership/investment agreement. Therefore, the tax benefits are conveyed to the investor through a contractual arrangement and an equity ownership interest meets the definition of a financial asset.

• The election of the FVO will not cause income recognition of tax credits before they are earned. Recognition in income of any benefit of the tax credits to be received over the term of the investment would preclude an entity from being eligible to elect the FVO for such an interest. Such preclusion is similar to the prohibition on electing the FVO for an equity investment that contains a significant component related to future services.

While the above discussion focuses on investments in affordable housing projects, the same concepts may be applied to investments in other tax-credit equity structures.
12.2.3 Interaction of ASC 825 With Other Codification Topics

12.2.3.1 General

<table>
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<td><strong>Interaction With Other Topics</strong></td>
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<tr>
<td><strong>15-6</strong> The Fair Value Option Subsections:</td>
</tr>
<tr>
<td>a. Do not affect any existing accounting literature that requires certain assets and liabilities to be carried at fair value</td>
</tr>
<tr>
<td>b. Do not establish requirements for recognizing and measuring dividend income, interest income, or interest expense</td>
</tr>
<tr>
<td>c. Do not eliminate disclosure requirements included in other Subtopics, including requirements for disclosures about fair value measurements included in Topic 820.</td>
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ASC 825-10-15-6 states that the FVO guidance in ASC 825 does not (1) affect any existing U.S. GAAP under which certain assets or liabilities must be recognized at fair value or (2) eliminate disclosure requirements of other Codification topics. However, incremental disclosures are required for items accounted for at fair value by using the FVO. See Section 12.5 for further discussion.

ASC 825-10-15-6 also indicates that ASC 825 does not address the recognition or measurement of dividend income, interest income, or expense on items recognized at fair value under the FVO. For further discussion of the recognition of interest on an interest-bearing financial instrument for which the FVO is elected, see Section 12.4.1.1.1.

12.2.3.2 Hybrid Instruments That Are Not Separated Under ASC 815-15

12.2.3.2.1 General

<table>
<thead>
<tr>
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<tr>
<td><strong>Fair Value Election for Hybrid Financial Instruments</strong></td>
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<tr>
<td><strong>25-4</strong> An entity that initially recognizes a hybrid financial instrument that under paragraph 815-15-25-1 would be required to be separated into a host contract and a derivative instrument may irrevocably elect to initially and subsequently measure that hybrid financial instrument in its entirety at fair value (with changes in fair value recognized in earnings and, if paragraph 825-10-45-5 is applicable, other comprehensive income). A financial instrument shall be evaluated to determine that it has an embedded derivative requiring bifurcation before the instrument can become a candidate for the fair value election.</td>
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| 25-5 The fair value election shall be supported by concurrent documentation or a preexisting documented policy for automatic election. That recognized hybrid financial instrument could be an asset or a liability and it could be acquired or issued by the entity. The fair value election is also available when a previously recognized financial instrument is subject to a remeasurement event (new basis event) and the separate recognition of an embedded derivative. The fair value election may be made instrument by instrument. For purposes of this paragraph, a remeasurement event (new basis event) is an event identified in generally accepted accounting principles, other than the recognition of an other-than-temporary impairment, or measurement of an impairment loss through earnings under Topic 321 on equity investments, that requires a financial instrument to be remeasured to its fair value at the time of the event but does not require that instrument to be reported at fair value on a continuous basis with the change in fair value recognized in earnings. Examples of remeasurement events are business combinations and significant modifications of debt as defined in Subtopic 470-50. |
ASC 815-15 (continued)

Pending Content (Transition Guidance: ASC 326-10-65-1)

25-5 The fair value election shall be supported by concurrent documentation or a preexisting documented policy for automatic election. That recognized hybrid financial instrument could be an asset or a liability and it could be acquired or issued by the entity. The fair value election is also available when a previously recognized financial instrument is subject to a remeasurement event (new basis event) and the separate recognition of an embedded derivative. The fair value election may be made instrument by instrument. For purposes of this paragraph, a remeasurement event (new basis event) is an event identified in generally accepted accounting principles, other than the recording of a credit loss under Topic 326, or measurement of an impairment loss through earnings under Topic 321 on equity investments, that requires a financial instrument to be remeasured to its fair value at the time of the event but does not require that instrument to be reported at fair value on a continuous basis with the change in fair value recognized in earnings. Examples of remeasurement events are business combinations and significant modifications of debt as defined in Subtopic 470-50.

25-6 The fair value election shall not be applied to the hybrid instruments described in paragraph 825-10-50-8.

Hybrid Instruments That Are Not Separated

30-1 An entity shall measure both of the following initially at fair value:
   a. A hybrid financial instrument that under paragraph 815-15-25-1 would be required to be separated into a host contract and a derivative instrument that an entity irrevocably elects to initially and subsequently measure in its entirety at fair value (with changes in fair value recognized in earnings)
   b. An entire hybrid instrument if an entity cannot reliably identify and measure the embedded derivative that paragraph 815-15-25-1 requires be separated from the host contract.

Fair Value Election

35-1 If an entity irrevocably elected to initially and subsequently measure a hybrid financial instrument in its entirety at fair value, changes in fair value for that hybrid financial instrument shall be recognized in earnings. Paragraph 815-20-25-71(a)(3) states that the entire contract shall not be designated as a hedging instrument pursuant to Subtopic 815-20.

Inability to Reliably Identify and Measure Embedded Derivative

35-2 If an entity cannot reliably identify and measure the embedded derivative that paragraph 815-15-25-1 requires be separated from the host contract, the entire contract shall be measured subsequently at fair value with gain or loss recognized in earnings. Paragraph 815-20-25-71(a)(4) states that the entire contract shall not be designated as a hedging instrument pursuant to Subtopic 815-20.

Under ASC 815-15-25-1, an entity may be required to bifurcate and separately account for an embedded derivative contained within a hybrid instrument. In lieu of such separation, ASC 815-15-25-4 allows an entity to account for the entire hybrid instrument at fair value, provided that the instrument is a financial asset or financial liability, with changes recognized in earnings and, if applicable, OCI. Further, ASC 815-15-30-1(b) and ASC 815-15-35-2 address the accounting in the unusual circumstance in which an entity is unable to reliably identify and separately measure the embedded derivative in a hybrid instrument that must be accounted for separately as a derivative instrument.
12.2.3.2.2 Fair Value Election

The fair value election in ASC 815-15 originated from the guidance in FASB Statement 155, which was issued before Statement 159 (the pre-Codification FVO guidance now contained in ASC 825). The fair value election in ASC 815-15 can be made on an instrument-by-instrument basis, or an entity can elect this option for all qualifying hybrid financial instruments on some other basis, such as an entity-wide policy decision or a type-of-instrument basis. In all scenarios, the fair value election under ASC 815-15 must be supported with appropriate concurrent documentation that eliminates any question regarding whether the entity elected to apply fair value measurement to a particular instrument.

For the following reasons, the fair value election in ASC 815-15 applies to a narrower population (scope) of items than the FVO in ASC 825:

- The fair value election in ASC 815-15 applies only to hybrid financial instruments for which bifurcation of an embedded derivative would otherwise be required. An entity that elects the FVO in ASC 825 is not required to determine that an embedded derivative would need to be accounted for separately under ASC 815-15.
- ASC 815-15-25-6 prohibits the fair value election for any hybrid instrument that is discussed in ASC 825-10-50-8, which describes 15 items for which public business entities are not required to provide fair value disclosures. The scope of ASC 825-10-50-8 is more restrictive than the scope of the FVO in ASC 825-10-15-4 and 15-5.

Like ASC 825, ASC 815-15 allows the fair value election for an eligible item only upon (1) initial recognition or (2) the occurrence of a subsequent remeasurement event (i.e., a subsequent remeasurement of the entire instrument at fair value under other U.S. GAAP). Therefore, under both ASC 815-15 and ASC 825, an entity is prohibited from making the fair value election upon determining that an embedded derivative that was previously not bifurcated under ASC 815-15 subsequently must be bifurcated (e.g., a hybrid financial instrument containing an embedded derivative that meets the net settlement condition in ASC 815-10-15-83(c) after initial recognition).

There are no situations for which an entity could make the fair value election for a hybrid instrument under ASC 815-15 but would be prohibited from electing the FVO for the same instrument under ASC 825. In addition, regardless of whether the entity uses ASC 815-15 or ASC 825 in applying fair value accounting, the hybrid financial instrument cannot be designated as a hedging instrument under ASC 815-20. Furthermore, the documentation and disclosure requirements related to the fair value election in ASC 815-15 are the same as those related to the FVO in ASC 825.

Connecting the Dots

Since the fair value election under ASC 815-15 applies to a narrower population of items than the FVO under ASC 825, entities can effectively disregard the fair value election guidance in ASC 815-15-25-4. While ASC 815-15 requires an entity to first determine that a hybrid financial instrument contains an embedded derivative for which bifurcation would otherwise be required under ASC 815-15, entities can bypass this assessment because — regardless of whether such bifurcation is required — the hybrid financial instruments that are eligible for the fair value election in ASC 815-15 are also eligible for the FVO in ASC 825 (and the FVO in ASC 825 can be elected regardless of whether an entity has identified an embedded derivative for which bifurcation would otherwise be required). Furthermore, the disclosure requirements applicable

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2 ASC 815-15-25-5 states that “the fair value election shall be supported by concurrent documentation or a preexisting documented policy for automatic election” (emphasis added). The term “concurrent documentation” is analogous to the term “contemporaneous documentation,” as used in the hedge accounting requirements of ASC 815. Therefore, the fair value election for hybrid financial instruments under ASC 815-15 must be documented at the time a hybrid financial instrument is acquired or issued or when a previously recognized hybrid financial instrument is subject to a remeasurement (new basis) event. If the documentation does not exist at that time, the FVO may not be elected. We believe that entities applying the guidance in ASC 815-15 on the fair value election would also be subject to the requirements related to the FVO in ASC 825.
to a hybrid financial instrument for which the fair value election is made under ASC 815-15 are consistent with the disclosure requirements of ASC 825. Regardless of whether an FVO election is made under ASC 815-15 or ASC 825, it is subject to the applicable incremental disclosure requirements for (1) derivatives in ASC 815 and (2) items for which the FVO has been elected in ASC 825. We believe that the guidance on fair value elections in ASC 815-15 (which was derived from Statement 155) was retained in U.S. GAAP because that guidance was available (and may have been used) before the effective date of Statement 159 (codified in ASC 825). Thus, entities may still have hybrid financial instruments that are being recognized at fair value in their entirety in accordance with ASC 815-15 because those instruments were issued before the effective date of the FVO guidance in ASC 825.

12.2.3.2.3 Inability to Reliably Identify and Measure Embedded Derivatives

The fair value election in ASC 815-15 is available only for hybrid financial instruments with an embedded derivative for which bifurcation would otherwise be required. (As discussed in Section 12.2.3.2.2, hybrid financial instruments that would qualify for the fair value election in ASC 815-15 would also qualify for the FVO in ASC 825, regardless of whether an entity has identified an embedded derivative for which bifurcation would otherwise be required.) However, there may be hybrid nonfinancial instruments that are not eligible for the fair value election in ASC 815-15 or the FVO in ASC 825 and for which the entity cannot reliably identify and measure the embedded derivative that must be bifurcated under ASC 815-15. ASC 815-15-30-1(b) and ASC 815-15-35-2 states that, in these circumstances, an entity should measure the entire hybrid instrument at fair value. The resulting accounting is the same as it would be if the entity had made the fair value election in ASC 815-15 or elected the FVO in ASC 825. Note that under no circumstance can such an instrument be designated as a hedging instrument under ASC 815-20.

Connecting the Dots

The provision of ASC 815-15-30-1(b) and ASC 815-15-35-2 that requires fair value accounting for a hybrid instrument for which the entity cannot reliably identify and measure the embedded derivative that the entity would otherwise be required to bifurcate is necessary because, for example, fair value accounting for a hybrid nonfinancial instrument under the fair value election in ASC 815-15 or the FVO in ASC 825 would be prohibited. In practice, however, this provision is rarely applied.

12.2.3.3 Other Codification Topics

Other Codification topics may give entities the option of measuring assets or liabilities at fair value through earnings. Such assets or liabilities include, but are not necessarily limited to, the following:

- Investments in debt securities that are classified as trading under ASC 320.
- Investments in equity securities without readily determinable fair values under ASC 321.
- Investments in life settlement contracts that are accounted for by using the fair value method under ASC 325-30.
- Classes of servicing assets or servicing liabilities that are accounted for by using the fair value measurement method in ASC 860-50.

An entity that elects fair value accounting for such assets or liabilities under a Codification topic other than ASC 825 only needs to comply with the disclosure requirements of that topic and is not subject to ASC 825’s FVO disclosure requirements. See further discussion in Section 12.5.1.
12.2.3.4 **NFP Entities**

**ASC 825-10**

*Application by Not-for-Profit Entities*

15-7 Not-for-profit entities (NFPs) shall apply the provisions of the Fair Value Option Subsections with the following modifications:

a. References to an income statement shall be replaced with references to a statement of activities, statement of changes in net assets, or statement of operations.

b. References to earnings shall be replaced with references to changes in net assets, except as indicated in (c).

c. Paragraph 954-825-45-1 explains that health care entities subject to Topic 954 shall report unrealized gains and losses on items for which the fair value option has been elected within the performance indicator or as a part of discontinued operations, as appropriate. Unlike other NFPs, health care entities subject to that Topic present performance indicators analogous to income from continuing operations. Consistent with the provisions of Subtopic 958-10, NFPs may present such gains and losses either within or outside of other intermediate measures of operations unless such gains or losses are part of discontinued operations. This includes intermediate measures of operations presented by NFPs other than health care entities and any additional intermediate measures of operations presented within the performance indicator by not-for-profit health care entities.

d. The disclosure requirements in paragraph 825-10-50-30 shall apply not only with respect to the effect on performance indicators or other intermediate measures of operations, if presented, but also with respect to the effect on the change in each of the net asset classes (without donor restrictions or with donor restrictions), as applicable.

ASC 825-10-15-7 explains the FVO presentation requirements for NFP entities, including health care entities, which do not present an income statement. ASC 825-10-15-7 also clarifies the disclosure requirements that apply to NFP entities that have elected the FVO. See Section 12.5 for further discussion of the FVO disclosure requirements.

12.3 **Recognition**

12.3.1 **Overall Guidance**

**ASC 825-10**

*Overall Guidance*

25-1 This Subtopic permits all entities to choose, at specified election dates, to measure eligible items at fair value (the fair value option).

25-2 The decision about whether to elect the fair value option:

a. Shall be applied instrument by instrument, except as discussed in paragraph 825-10-25-7

b. Shall be irrevocable (unless a new election date occurs, as discussed in paragraph 825-10-25-4)

c. Shall be applied only to an entire instrument and not to only specified risks, specific cash flows, or portions of that instrument.

An entity may decide whether to elect the fair value option for each eligible item on its election date. Alternatively, an entity may elect the fair value option according to a preexisting policy for specified types of eligible items.

25-3 Upfront costs and fees related to items for which the fair value option is elected shall be recognized in earnings as incurred and not deferred.
12.3.1.1 Election of the FVO

An entity is permitted to elect the FVO for eligible financial assets and financial liabilities (see Section 12.2.1) on the election dates discussed in Section 12.3.2. ASC 825 provides little guidance on the documentation an entity is required to maintain to support its election of the FVO but indicates that the decision to elect the FVO should be made as of the election date for each eligible item. An entity also may establish an automatic election policy for certain eligible items. For example, an entity may document in a written policy that it will elect the FVO for all single-family mortgages that it originates. In deciding to permit entities to elect the FVO, the Board noted that maintaining evidence of compliance with the election requirements of ASC 825 is a matter of internal control. Although ASC 825 leaves room for discretion regarding documentation, an entity that does not have a well-developed preexisting policy for election should document evidence of the election concurrently with the recognition or remeasurement of eligible items.

12.3.1.1.1 Application on an Instrument-by-Instrument Basis

In the absence of specific exceptions addressed in ASC 825-10-25-7, an entity can elect the FVO on an instrument-by-instrument basis. This election is made on the basis of the unit of account for eligible instruments under other applicable U.S. GAAP. Thus, entities may elect the FVO for a single eligible item without electing the FVO for other identical items. Entities also have the flexibility to establish an automatic election policy for certain eligible items of an identical or similar nature. Section 12.3.1.1.1.1 includes additional discussion of the unit of account with respect to FVO elections, including exceptions to the general ability to elect the FVO on an instrument-by-instrument basis.

The FVO election approach applied will affect the nature and extent of documentation related to FVO elections. For example, if an entity makes an FVO election decision each time it initially recognizes an eligible item within a group of identical or similar eligible items, the entity would need to concurrently document the FVO elections more frequently than an entity that has a policy of always electing the FVO for such an item. Further, this documentation would need to be sufficiently clear on the items for which the FVO has been elected. An entity that does not apply the FVO to all eligible items within a group of similar eligible items would also be required to provide additional disclosures (see Section 12.5.3).

In all scenarios, an entity must support its FVO election under ASC 825 with appropriate concurrent documentation that eliminates any question regarding whether the entity elected to apply fair value measurement to a particular instrument.
12.3.1.1.1 Unit of Account

ASC 825-10

Unit of Accounting

25-7 The fair value option may be elected for a single eligible item without electing it for other identical items with the following four exceptions:

a. If multiple advances are made to one borrower pursuant to a single contract (such as a line of credit or a construction loan) and the individual advances lose their identity and become part of a larger loan balance, the fair value option shall be applied only to the larger balance and not to each advance individually.

b. If the fair value option is applied to an investment that would otherwise be accounted for under the equity method of accounting, it shall be applied to all of the investor's financial interests in the same entity (equity and debt, including guarantees) that are eligible items.

c. If the fair value option is applied to an eligible insurance or reinsurance contract, it shall be applied to all claims and obligations under the contract.

d. If the fair value option is elected for an insurance contract (base contract) for which integrated or nonintegrated contract features or coverages (some of which are called riders) are issued either concurrently or subsequently, the fair value option also must be applied to those features or coverages. The fair value option cannot be elected for only the nonintegrated contract features or coverages, even though those features or coverages are accounted for separately under Subtopic 944-30. Paragraph 944-30-35-30 defines a nonintegrated contract feature in an insurance contract. For purposes of applying this Subtopic, neither an integrated contract feature or coverage nor a nonintegrated contract feature or coverage qualifies as a separate instrument.

25-10 The fair value option need not be applied to all instruments issued or acquired in a single transaction (except as required by paragraph 825-10-25-7(a) through (b)). For example, investors in shares of stock and registered bonds might apply the fair value option to only some of the shares or bonds issued or acquired in a single transaction. For this purpose, an individual bond is considered to be the minimum denomination of that debt security.

25-11 A financial instrument that is legally a single contract may not be separated into parts for purposes of applying the fair value option. In contrast, a loan syndication arrangement may result in multiple loans to the same borrower by different lenders. Each of those loans is a separate instrument, and the fair value option may be elected for some of those loans but not others.

25-12 An investor in an equity security may elect the fair value option for its entire investment in that equity security, including any fractional shares issued by the investee (for example, fractional shares that are acquired in a dividend reinvestment program).

25-13 For the issuer of a liability issued with an inseparable third-party credit enhancement (for example, debt that is issued with a contractual third-party guarantee), the unit of accounting for the liability measured or disclosed at fair value does not include the third-party credit enhancement. This paragraph does not apply to the holder of the issuer's credit-enhanced liability or to any of the following financial instruments or transactions:

a. A credit enhancement granted to the issuer of the liability (for example, deposit insurance provided by a government or government agency)

b. A credit enhancement provided between reporting entities within a consolidated or combined group (for example, between a parent and its subsidiary or between entities under common control).
An entity can generally elect the FVO for a single eligible item without electing it for other identical items (with four exceptions addressed in ASC 825-10-25-7, which are discussed below). Note that the determination of what constitutes a “single eligible item” is made on the basis of the unit of account under U.S. GAAP. The unit of account is generally determined under other applicable Codification topics; however, ASC 825 does contain the following unit-of-account guidance that applies to application of the FVO:

- The FVO may be applied to a “host financial instrument resulting from the separation of an embedded nonfinancial derivative from a nonfinancial hybrid instrument” (ASC 825-10-15-4(f)).
- An “individual bond is considered . . . the minimum denomination of [a] debt security” (ASC 825-10-25-10).
- A “financial instrument that is legally a single contract may not be separated” into its component parts when the FVO is applied (ASC 825-10-25-11).
- The unit of account for a liability issued with an inseparable third-party credit enhancement “does not include the third-party credit enhancement” (ASC 825-10-25-13).

**Connecting the Dots**

In applying ASC 825-10-25-11, which states, in part, that “[a] financial instrument that is legally a single contract may not be separated into parts for purposes of applying the fair value option,” an entity must consider the definition of the term “freestanding financial instrument” in the ASC master glossary. For example, a debt instrument with a $1 million principal amount and a warrant on 100,000 shares of common stock may be entered into with a single investor and documented in the same contract. If the warrant is legally detachable and separately exercisable, the debt instrument and warrant would individually represent freestanding financial instruments (i.e., the debt instrument would be considered an individual contract under ASC 825-10-25-11). The entity could therefore apply the FVO to its liability related to the $1 million debt instrument provided that none of the FVO exceptions in ASC 825-10-15-5 are applicable. The warrant would be separately evaluated as a liability or equity instrument under other applicable U.S. GAAP (e.g., ASC 480, ASC 815, and ASC 815-40). The entity could not, however, apply the FVO to only $500,000 of the $1 million principal amount of debt, because the entire principal amount represents a single unit of account and ASC 825-10-25-11 prohibits the election of the FVO for only a portion of the amount of an individual bond. If, however, the entity had entered into the aforementioned contract with 10 different investors, it could individually make the FVO election for the $1 million principal amount of the debt component of each of the 10 different contracts (e.g., it could elect the FVO for the $1 million debt component related to five investors and not elect the FVO for the $1 million debt component for the other five investors).

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3 An entity may elect the FVO for one eligible debt instrument (such as an individual loan or an individual bond) and not elect the FVO for a separate but identical debt instrument, provided that the debt instrument reflects a separate and distinct contract (i.e., the debt instrument has a different counterparty or is legally detachable and separately transferable). For instance, the FVO may be applied to only some of the individual bonds issued or acquired in a single transaction even though the terms of each bond are identical. If a group of lenders jointly fund a loan to a single borrower and each lender loans a specific amount to the borrower and has the right to demand repayment from the borrower, the loan from each lender is considered separate and distinct from the loans from other lenders even if each of the loans forms part of the same overall loan syndication agreement. Thus, ASC 825-10-25-11 permits election of the FVO for each loan in a loan syndication arrangement in which the loans are made to the same borrower by different lenders.
ASC 825-10-25-7 describes the following four situations in which it is not appropriate to elect the FVO for only a single eligible item without electing the FVO for other identical items:

- **Multiple advances to a single borrower** — “If multiple advances are made to one borrower pursuant to a single contract (such as a line of credit or a construction loan) and the individual advances lose their identity and become part of a larger loan balance, the [FVO] shall be applied only to the larger balance and not to each advance individually.” See Example 12-9 below for a related illustration.

- **Equity method investments** — If the FVO “is applied to an investment that would otherwise be accounted for” by using the equity method, the FVO must be applied to all of the investor’s financial interests in the investee that are eligible for the FVO (e.g., equity, debt, guarantees).

- **Insurance or reinsurance contracts** — If the FVO “is applied to an eligible insurance or reinsurance contract,” it must be applied to all “claims and obligations under the contract.”

- **Insurance contracts with integrated or nonintegrated contract features or coverages** — If the FVO “is elected for an insurance contract (base contract) for which integrated or nonintegrated contract features or coverages (some of which are called riders) are issued either concurrently or subsequently, the [FVO] also must be applied to those features or coverages. The [FVO] cannot be elected for only the nonintegrated contract features or coverages, even though those features or coverages are accounted for separately under Subtopic 944-30.”

**Example 12-9**

**ELECTING THE FVO FOR PORTIONS OF A FINANCIAL INSTRUMENT THAT INCLUDES MULTIPLE LENDINGS TO THE SAME BORROWER**

Entity F has a $5 million line-of-credit agreement with Bank A. On March 1, 20X7, F draws $500,000 on its line of credit and chooses not to elect the FVO. On April 1, 20X7, F draws another $1 million. Because the $1 million is added to the $500,000 and becomes part of the larger balance, the FVO may not be elected for the $1 million. When F chose not to elect the FVO for the $500,000, it also chose not to elect the FVO for any subsequent draws on that line of credit. Under ASC 825-10-25-4, that election is irrevocable unless a new election date occurs.

12.3.1.1.2 Application on an Irrevocable Basis

Once an entity makes an FVO election for an eligible item, fair value accounting is required and may not be revoked unless a new election date occurs under ASC 825-10-25-4. See Section 12.3.2 for discussion of election dates.

12.3.1.1.3 Application to an Entire Instrument

ASC 825-10-25-2(c) requires entities to apply the FVO “to an entire instrument and not to only specified risks, specific cash flows, or portions of that instrument.” There is one exception to this requirement. Specifically, as noted in ASC 825-10-15-4(f), the FVO may be applied to a “host financial instrument resulting from the separation of an embedded nonfinancial derivative from a nonfinancial hybrid instrument” (see Section 12.2.1.4 for more information). See Section 12.3.1.1.1.1 for more information about the unit of account.
12.3.1.1.3.1 Accrued Interest on an Interest-Bearing Financial Instrument

An entity cannot separately elect the FVO for accrued interest (receivable or payable) on an interest-bearing financial asset or financial liability. Similarly, an entity cannot elect the FVO for an interest-bearing financial asset or financial liability and exclude the accrued interest component from such election. (Accrued interest simply represents one or more future interest cash flows of an interest-bearing financial asset or financial liability that have already been earned.) Rather, in accordance with ASC 825-10-25-2(c), an entity must either (1) elect the FVO for an interest-bearing financial asset or financial liability that includes any accrued interest or (2) not elect the FVO for any component of an interest-bearing financial asset or financial liability.

Certain Codification topics permit entities to defer and amortize up-front costs over the life of an interest-bearing financial asset or financial liability. However, if an entity elects the FVO, any such up-front costs and fees related to the asset or liability that the entity incurs must be recognized in earnings as incurred and not deferred. See Section 12.3.1.2 below for more information.

12.3.1.2 Up-Front Costs

ASC 825-10-25-3 requires that up-front costs and fees related to items for which the FVO is elected be recognized in earnings as incurred and not deferred. This requirement is consistent with ASC 820-10-35-9B, which indicates that transaction costs are not part of a fair value measurement. Thus, loan origination fees and costs will be recognized in earnings as incurred and not capitalized under ASC 310-20. Similarly, acquisition costs will not be capitalized when the FVO is elected for an insurance contract.

As a result of the requirement to expense (or recognize in income), rather than defer, incremental direct costs or origination fees or costs associated with the origination or acquisition of an interest-bearing financial instrument that is accounted for at fair value by using the FVO, the reported amounts of interest expense or interest income (if separately reported) will differ from those that are reported when the same asset or liability is accounted for at amortized cost. See Section 12.4.1.1.1.2 for further discussion of the measurement of interest income or expense related to an interest-bearing financial instrument for which the FVO is elected.
12.3.2 Election Dates

12.3.2.1 General

ASC 825-10

Election Dates

25-4 An entity may choose to elect the fair value option for an eligible item only on the date that one of the following occurs:

a. The entity first recognizes the eligible item.

b. The entity enters into an eligible firm commitment.

c. Financial assets that have been reported at fair value with unrealized gains and losses included in earnings because of specialized accounting principles cease to qualify for that specialized accounting (for example, a transfer of assets from a subsidiary subject to Subtopic 946-10 to another entity within the consolidated reporting entity not subject to that Subtopic).

d. The accounting treatment for an investment in another entity changes because the investment becomes subject to the equity method of accounting.

e. An event that requires an eligible item to be measured at fair value at the time of the event but does not require fair value measurement at each reporting date after that, excluding the recognition of impairment under lower-of-cost-or-market accounting or other-than-temporary impairment or accounting for equity securities in accordance with Topic 321.

Pending Content (Transition Guidance: ASC 326-10-65-1)

25-4 An entity may choose to elect the fair value option for an eligible item only on the date that one of the following occurs:

a. The entity first recognizes the eligible item.

b. The entity enters into an eligible firm commitment.

c. Financial assets that have been reported at fair value with unrealized gains and losses included in earnings because of specialized accounting principles cease to qualify for that specialized accounting (for example, a transfer of assets from a subsidiary subject to Subtopic 946-10 to another entity within the consolidated reporting entity not subject to that Subtopic).

d. The accounting treatment for an investment in another entity changes because the investment becomes subject to the equity method of accounting.

e. An event that requires an eligible item to be measured at fair value at the time of the event but does not require fair value measurement at each reporting date after that, excluding the recognition of impairment under lower-of-cost-or-market accounting or accounting for securities in accordance with either Topic 321 on investments — equity securities or Topic 326 on measurement of credit losses.

25-5 Some of the events that require remeasurement of eligible items at fair value, initial recognition of eligible items, or both, and thereby create an election date for the fair value option as discussed in paragraph 825-10-25-4(e) are:

a. Business combinations, as defined in Subtopic 805-10

b. Consolidation or deconsolidation of a subsidiary or VIE

c. Significant modifications of debt, as defined in Subtopic 470-50.
In accordance with ASC 825-10-25-4, an entity can elect the FVO only upon (1) the initial recognition of an eligible item or the date an entity enters into a firm commitment or (2) the occurrence of a qualifying event. Those qualifying events are specified in the items in ASC 825-10-25-4(c)–(e) and include the following:

- Fair value accounting ceases under specialized accounting guidance.
- An equity investment becomes subject to the equity method.
- An event occurs that “requires an eligible item to be measured at fair value at the time of the event but does not require fair value measurement at each reporting date after that, excluding the recognition of impairment” on financial assets not accounted for at fair value. (ASC 820-10-20 defines these events as “remeasurement events.”)

Upon the occurrence of any of these qualifying events, an entity has, in addition to the ability to elect the FVO, the option to cease applying the FVO to an eligible item to which it was previously applied. See Section 12.3.2.2 for interpretive guidance on these election dates. See Section 12.5.4 for discussion of the incremental disclosures an entity is required to provide when electing the FVO upon the occurrence of the qualifying events in ASC 825-10-25-4(d) and (e).

In addition, the transition provisions of certain ASUs may allow for a one-time FVO election. For example, ASU 2019-05 allows entities to elect the FVO in lieu of applying the guidance in ASC 326 on expected credit losses.

### Connecting the Dots

As discussed in Section 12.2.3.3, other Codification topics may give entities the option of measuring an asset or liability at fair value through earnings. An entity should consult such other U.S. GAAP to determine whether it may elect fair value accounting after initial recognition of the related item. For example, ASC 321, as amended by ASU 2018-03, allows an entity that is measuring an equity security without a readily determinable fair value, and that is using the measurement alternative, to change its measurement approach to a fair value method in accordance with ASC 820. This election would be irrevocable and would apply to that security and all identical or similar investments of the same issuer. Once an entity makes this election, the entity should measure all future purchases of identical or similar investments of the same issuer by using a fair value method in accordance with ASC 820.

### 12.3.2.2 Interpretive Guidance

#### 12.3.2.2.1 Entity Enters Into an Eligible Firm Commitment

ASC 825-10-25-4(b) allows an entity to elect the FVO on the date it “enters into an eligible firm commitment.” We believe that this date is that on which the definition of a firm commitment is met. This date could not occur before the date on which the commitment is binding on both parties and is legally enforceable.

#### 12.3.2.2.2 Fair Value Accounting Under Specialized Accounting Guidance Ceases

Under ASC 825-10-25-4(c), an entity can elect the FVO when “financial assets that have been reported at fair value with unrealized gains and losses included in earnings because of specialized accounting principles cease to qualify for that specialized accounting.” This new election date may be relevant when an entity ceases to be an investment company under ASC 946, which can occur for a number of reasons.
12.3.2.2.3 Matters Related to Equity Method Accounting

12.3.2.2.3.1 Investment Becomes Subject to Equity Method of Accounting

Under ASC 825-10-25-4(d), if an entity’s investment in another entity “becomes subject to the equity method of accounting,” the entity may elect the FVO for its investment in lieu of applying the equity method. An investment could become subject to the equity method for various reasons, including (1) an acquisition of an additional interest in an investee that causes the investor to obtain significant influence over the investee; (2) a change in an investee’s governing provisions in such a way that an investor obtains significant influence over the investee; (3) an investee’s repurchase of its outstanding equity shares, resulting in an increase in an investor’s ownership percentage in the investee in such a way that the investor obtains significant influence over the investee; or (4) an investor’s loss of control, but retention of significant influence, over an investee. If an investor elects the FVO when its investment becomes subject to the equity method of accounting, the investor must elect the FVO for all other interests in the investee that are eligible items in accordance with ASC 825-10-25-7(b). For this purpose, we believe that other preexisting interests in the investee that would not otherwise become subject to the equity method of accounting are not eligible items unless they are subject to another remeasurement event as of the date on which the entity becomes subject to the equity method of accounting.

12.3.2.2.3.2 Investment Is No Longer Subject to Equity Method of Accounting

The FVO election dates listed in ASC 825-10-25-4 do not include the date on which an investor loses significant influence over an investee (through either a decline in the investor’s holding of voting stock or other changes in circumstances that cause an investor to lose its ability to influence an investee’s policies). Thus, if an investor concludes that it would no longer be subject to the equity method of accounting for an investee, it does not have a new election date for the FVO under ASC 825. Table 12-2 describes how an investor would account for the retained investment if it determines that it loses significant influence and therefore is no longer subject to the equity method of accounting.

### Table 12-2

<table>
<thead>
<tr>
<th>Accounting While Having Significant Influence</th>
<th>Accounting for Retained Investment After Losing Significant Influence</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity method of accounting</td>
<td>The investor should account for the equity investment in accordance with ASC 321. If the investment has a readily determinable fair value, it must be recognized at fair value, with changes in fair value reported in earnings. If the investment does not have a readily determinable fair value, the investor can either account for the equity investment at fair value, with changes in fair value reported in earnings, or elect the measurement alternative in ASC 321-10-35-2. The guidance in U.S. GAAP is not clear on whether, when the measurement alternative is elected, the investor should account for observable price changes that necessitate its discontinuation of the equity method immediately before discontinuing the application of equity method accounting under ASC 323. The EITF is currently addressing this topic in Issue 19-A.</td>
</tr>
<tr>
<td>FVO was elected</td>
<td>The investor must continue to apply the FVO to any retained investment that was previously accounted for at fair value by using the FVO, because the loss of significant influence does not warrant a new election date.</td>
</tr>
</tbody>
</table>

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4 This would also represent a remeasurement event under ASC 825-10-25-4(e).
12.3.2.2.4  Remeasurement Events

12.3.2.2.4.1  General

<table>
<thead>
<tr>
<th>ASC Master Glossary</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Remeasurement Event</strong></td>
</tr>
<tr>
<td>A remeasurement (new basis) event is an event identified in other authoritative accounting literature, other than the recognition of an other-than-temporary impairment, that requires a financial instrument to be remeasured to its fair value at the time of the event but does not require that financial instrument to be reported at fair value continually with the change in fair value recognized in earnings. Examples of remeasurement events are business combinations and significant modifications of debt as discussed in paragraph 470-50-40-6.</td>
</tr>
</tbody>
</table>

**Note:** The following definition is Pending Content; see Transition Guidance in 326-10-65-1.

In accordance with ASC 825-10-25-4(e), an entity may make a new FVO election upon the occurrence of a remeasurement event. Thus, upon a remeasurement event, an entity can elect the FVO for, or cease applying it to, an eligible item. ASC 825-10-25-5 lists examples of remeasurement events. See below for further discussion of certain types of remeasurement events.

12.3.2.2.4.2  Initial Consolidation of a Subsidiary or VIE

The initial consolidation of a subsidiary or VIE represents a remeasurement event only for eligible financial assets or financial liabilities that are initially recognized at fair value. For example, under ASC 810-10-30-1 and ASC 810-10-30-3, assets and liabilities recognized upon initial consolidation of a VIE may not be measured at fair value (i.e., the amounts are recognized on the basis of their historical carrying amounts). In these situations, a remeasurement event allowing for a new FVO election does not exist. Further, we believe that, in initial consolidation transactions among entities under common control, it would not be appropriate for the receiving entity to elect to cease applying the FVO to elected items of the transferring entity, since common-control transactions do not meet the definition of a remeasurement event in ASC 825-10-20.

12.3.2.2.4.3  Debtors’ and Creditors’ Considerations When a Loan Is Refinanced or Modified

The determination of whether an entity’s refinancing or modification of a loan (in situations other than a troubled debt restructuring) qualifies under ASC 825-10-25-4(e) as a remeasurement event for the borrower or creditor depends on the facts and circumstances. Paragraph A15 of the Basis for Conclusions of FASB Statement 159 states:

When a contract is modified (or a rider added to it) after it has been initially recognized, the question arises as to whether that modification would permit election of the fair value option for the related asset or liability. The Board decided that the availability of the fair value option should be based on whether, under GAAP, the modification is accounted for as the continuation of the original contract or as the termination of the original contract and the origination of a new contract. If the modification is considered the origination of a new contract, the fair value option could be elected on the date of its initial recognition. Otherwise, the entity’s previous decision about electing the fair value option for the original contract would govern the accounting for the continuation of that original contract.
12.3.2.2.4.3.1 Debtor’s Evaluation

**ASC 470-50**

**Modifications and Exchanges**

40-10 From the debtor’s perspective, an exchange of debt instruments between or a modification of a debt instrument by a debtor and a creditor in a nontroubled debt situation is deemed to have been accomplished with debt instruments that are substantially different if the present value of the cash flows under the terms of the new debt instrument is at least 10 percent different from the present value of the remaining cash flows under the terms of the original instrument. If the terms of a debt instrument are changed or modified and the cash flow effect on a present value basis is less than 10 percent, the debt instruments are not considered to be substantially different, except in the following two circumstances:

a. A modification or an exchange affects the terms of an embedded conversion option, from which the change in the fair value of the embedded conversion option (calculated as the difference between the fair value of the embedded conversion option immediately before and after the modification or exchange) is at least 10 percent of the carrying amount of the original debt instrument immediately before the modification or exchange.

b. A modification or an exchange of debt instruments adds a substantive conversion option or eliminates a conversion option that was substantive at the date of the modification or exchange. (For purposes of evaluating whether an embedded conversion option was substantive on the date it was added to or eliminated from a debt instrument, see paragraphs 470-20-40-7 through 40-9.)

ASC 470-50 indicates that a modification of an existing debt instrument or an exchange of debt instruments is an extinguishment of the original debt instrument if (1) the modification or exchange is not a troubled debt restructuring and (2) the new debt instrument is substantially different from the existing debt instrument. If a debt instrument has been refinanced or modified in such a way that it is substantially different from the original instrument, a remeasurement under ASC 825 has occurred and the FVO could be elected (or no longer applied if it was previously elected).

If the modification represents a troubled debt restructuring, the debt instrument is not considered a new instrument and, therefore, a new election date for the FVO is not available.

12.3.2.2.4.3.2 Creditor’s Evaluation

**ASC 310-20**

**Loan Refinancing or Restructuring**

35-9 If the terms of the new loan resulting from a loan refinancing or restructuring other than a troubled debt restructuring are at least as favorable to the lender as the terms for comparable loans to other customers with similar collection risks who are not refinancing or restructuring a loan with the lender, the refinanced loan shall be accounted for as a new loan. This condition would be met if the new loan’s effective yield is at least equal to the effective yield for such loans and modifications of the original debt instrument are more than minor. Any unamortized net fees or costs and any prepayment penalties from the original loan shall be recognized in interest income when the new loan is granted. The effective yield comparison considers the level of nominal interest rate, commitment and origination fees, and direct loan origination costs and would also consider comparison of other factors where appropriate, such as compensating balance arrangements.

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5 ASC 470-50 provides guidance on calculating the present value of cash flows for the 10 percent test.
ASC 310-20 (continued)

<table>
<thead>
<tr>
<th>Pending Content (Transition Guidance: ASC 326-10-65-1)</th>
</tr>
</thead>
</table>

**35-9** If the terms of the new loan resulting from a loan refinancing or restructuring, in which the refinancing or restructuring is not itself a troubled debt restructuring, are at least as favorable to the lender as the terms for comparable loans to other customers with similar collection risks who are not refinancing or restructuring a loan with the lender, the refinanced loan shall be accounted for as a new loan. This condition would be met if the new loan’s effective yield is at least equal to the effective yield for such loans and modifications of the original debt instrument are more than minor. Any unamortized net fees or costs and any prepayment penalties from the original loan shall be recognized in interest income when the new loan is granted. The effective yield comparison considers the level of nominal interest rate, commitment and origination fees, and direct loan origination costs and would also consider comparison of other factors where appropriate, such as compensating balance arrangements.

**35-10** If the refinancing or restructuring does not meet the condition set forth in the preceding paragraph or if only minor modifications are made to the original loan contract, the unamortized net fees or costs from the original loan and any prepayment penalties shall be carried forward as a part of the net investment in the new loan. In this case, the investment in the new loan shall consist of the remaining net investment in the original loan, any additional amounts loaned, any fees received, and direct loan origination costs associated with the refinancing or restructuring.

ASC 310-20 addresses when an entity should consider a refinancing or restructuring of a loan receivable to represent a “new loan” for accounting purposes. (This guidance is used in determining how to recognize unamortized net fees or costs and any prepayment penalties from the original loan.) An entity should apply this guidance in determining whether a refinancing or restructuring of a loan receivable in a nontroubled situation represents a remeasurement event under ASC 825-10-25-4(e). If the two criteria in ASC 310-20-35-9 are met in a refinancing or modification of a loan receivable, a remeasurement event under ASC 825 has occurred and the FVO can be elected (or no longer applied if it was previously elected). Otherwise, as stated in ASC 310-20-35-10, the refinanced or restructured loan receivable is not considered a new loan and a remeasurement event under ASC 825 therefore has not occurred.

If the refinancing or restructuring represents a troubled debt restructuring, the loan receivable is not considered a new instrument and, accordingly, a new election date for the FVO is not available.

### 12.3.3 Differences Between FVO Election for Investors and That for Investees

#### 12.3.3.1 Consolidated and Separate Financial Statements

<table>
<thead>
<tr>
<th>ASC 825-10</th>
</tr>
</thead>
</table>

**Consolidation**

**25-6** An acquirer, parent, or primary beneficiary decides whether to apply the fair value option to eligible items of an acquiree, subsidiary, or consolidated VIE, but that decision applies only in the consolidated financial statements. Fair value option choices made by an acquired entity, subsidiary, or VIE continue to apply in separate financial statements of those entities if they issue separate financial statements.

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6 ASC 310-20-35-11 provides guidance on how a creditor should evaluate whether a modification of the terms of a debt instrument as a result of a refinancing or restructuring (other than a troubled debt restructuring) is “more than minor” under ASC 310-20-35-9.
Upon a business combination or consolidation of a VIE, the acquirer, parent, or primary beneficiary may elect whether to apply the FVO in its consolidated financial statements provided that the initial consolidation of the acquiree, subsidiary, or consolidated VIE represents a remeasurement event (see Section 12.3.2.4.2 for more information). However, for the separate financial statements, the acquired entity, subsidiary, or VIE cannot make or change any FVO election unless pushdown accounting under ASC 805 is applied as of the date of the change-of-control event. Thus, a parent and a subsidiary may have different accounting bases for an eligible asset or liability of the subsidiary (i.e., the FVO has been elected in the consolidated financial statements but not in the separate financial statements of the subsidiary).

ASC 825-10-25-6 only specifically addresses the FVO election as of the date of a change-of-control event (e.g., when an acquirer obtains control of an acquiree in a business combination). Thus, questions have arisen regarding whether the FVO can be elected in the consolidated financial statements upon a subsidiary's initial recognition of an eligible item if the subsidiary does not elect the FVO in its separate financial statements. Although an FVO election for the consolidated financial statements is generally consistent with that for a subsidiary's separate financial statements, we believe that it is acceptable for the FVO election to be made in the consolidated financial statements without being made in the subsidiary's separate financial statements. Similarly, we believe that it is generally acceptable for a subsidiary to elect the FVO for an eligible item even if that same election is not made in the parent's consolidated financial statements. (However, such situations are not expected to be common.) These potential differences between the FVO election in the consolidated financial statements and that in the subsidiary's separate financial statements may arise when the FVO is not elected on the basis of management's intent.

12.3.3.2 Equity Method Investees

As discussed in Section 12.2.1.1.1, an investor can apply the FVO to an equity method investee without needing to “look through” to the investee's assets and liabilities to determine whether they are financial in nature. However, when the equity method of accounting is applied to an investee, an investor may not, in determining equity method earnings and losses, (1) elect the FVO for otherwise eligible financial assets and financial liabilities of the investee (e.g., elect the FVO at the investee level and therefore adjust the reported results of the investee) or (2) “unwind” the investee's FVO elections (e.g., adjust the reported results of the investee to exclude mark-to-market adjustments to the investee's financial assets or financial liabilities for which the investee elected the FVO).

12.4 Presentation

12.4.1 Statement of Comprehensive Income

12.4.1.1 General

<table>
<thead>
<tr>
<th>ASC 825-10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Statement of Comprehensive Income</td>
</tr>
<tr>
<td>45-4 A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings (or another performance indicator if the business entity does not report earnings) at each subsequent reporting date.</td>
</tr>
</tbody>
</table>

ASC 825-10-45-4 states that the changes in fair value of an item for which the FVO is elected should be recognized in net income (or another performance indicator if an entity does not report net income). However, see Section 12.4.1.2 for discussion of the recognition of a component of the change in fair value of a financial liability in OCI.
12.4.1.1.1 Presentation of Interest on Interest-Bearing Financial Instruments Accounted for at Fair Value Through Earnings

12.4.1.1.1 General

Under U.S. GAAP, an entity is not required to separately present, in its income statement, interest income or interest expense for interest-bearing financial assets or financial liabilities accounted for at fair value through earnings, unless (1) the entity must do so in accordance with regulatory guidance or (2) it is industry practice to do so. However, the entity may elect, as an accounting policy, to present interest income or interest expense separately from other changes in the fair value of financial instruments measured at fair value through earnings. This election would apply to interest-bearing financial instruments that are measured at fair value through earnings under the FVO in ASC 825 or ASC 815, as well as interest-bearing financial instruments that are measured at fair value under other relevant GAAP (e.g., trading debt securities under ASC 320).

The following U.S. GAAP guidance indicates that separate presentation of interest is a policy election:

- ASC 825-10-50-28(e)(2), which requires disclosure of the aggregate fair value of loans in nonaccrual status held as assets, and for which the FVO has been elected, if the “entity’s policy is to recognize interest income separately from other changes in fair value.”
- ASC 325-40-15-7, which notes that “it is practice for certain industries (such as banks and investment companies) to report interest income as a separate item in their income statements, even though the investments are accounted for at fair value.”

If an entity’s elected accounting policy related to separate recognition of interest income or interest expense is considered significant, the entity should disclose that policy in accordance with ASC 235-10-50-1. Section 12.4.1.1.1.2 contains guidance on how to measure interest income or interest expense when it is separately presented in the income statement for an interest-bearing financial instrument recognized at fair value through earnings.

12.4.1.1.1.2 Measurement

If an entity elects, as an accounting policy, to separately present interest income or interest expense on an interest-bearing financial instrument accounted for at fair value through earnings, the entity should, with one exception, include amortization or accretion of any premium or discount on the instrument as part of the separately reported interest income or interest expense. If the fair value initially recognized for an interest-bearing financial instrument (e.g., debt) differs from the principal amount due at maturity (“par”), this difference is a premium or discount that should be amortized or accreted. An entity should recognize the amortization or accretion in interest income or interest expense if it is separately presented. Under ASC 320-10-35-4 and ASC 325-40-35-2, the method used to measure interest income or interest expense on an interest-bearing financial instrument (including any amortization or accretion of a premium or discount) should be the same regardless of the measurement attribute (e.g., amortized cost) used to measure the financial instrument. Thus, the premium or discount should be amortized by using the interest method that would have applied to the interest-bearing financial asset or financial liability if it had not been recognized at fair value through earnings.

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7 Industry or regulatory guidance may require that certain entities separately present interest from other changes in fair value for certain interest-bearing financial instruments. For example, bank holding companies, brokers and dealers in securities, and investment companies generally present interest separately from other changes in fair value in their income statements.
8 ASC 948-310-35-2 establishes interest recognition guidance for HFS mortgage loans. That guidance precludes an entity from amortizing purchase discounts. See further discussion in Example 12-11.
The guidance above does not apply to the following:

- The portion of the difference between fair value and par at inception attributable to embedded features that are not indexed to interest rates or the issuer’s own credit (e.g., an in-the-money option that permits the holder to convert the debt instrument into a fixed number of the issuer’s equity shares). Entities should exclude such features from the discount or premium to be accreted or amortized.

- Any transaction costs and fees, such as debt issuance costs, origination costs, and origination fees (i.e., up-front costs and fees) are not part of the initial measurement of a financial instrument that is recognized at fair value and therefore are not included in any premium or discount of the financial instrument in accordance with ASC 825-10-25-3. That is, the interest method is used only for applicable discounts and premiums since up-front costs and fees are recognized in earnings as they are incurred or received (see Section 12.3.1.2 for discussion of the initial recognition of up-front costs and Section 12.4.1.1.2 for discussion of the income statement presentation of fees received and costs incurred that are associated with the origination of loans receivable).

Example 12-10

Measurement of Interest Income on Acquired Loans With Deteriorated Credit Quality That Are Recognized at Fair Value Through Earnings

Entity G acquires a portfolio of loans from a third party at a significant discount (at a transaction price equal to fair value) and has elected to account for the loans at fair value through earnings under the FVO in ASC 825. In accordance with G’s previously elected accounting policy, G separately presents interest income on these loans in its income statement.

If G had not elected to account for the loans under the FVO, a portion of the loans would have been accounted for under ASC 310-30 (which addresses the accounting for acquired loans with deteriorated credit quality) and the remaining portion would have been accounted for under ASC 310-20.

On the basis of these facts, G should measure interest income on the loans by applying ASC 310-30 to the portion of the portfolio that would have otherwise been accounted for under that guidance and applying ASC 310-20 to measure interest income on the remaining portion of the loan portfolio. In addition, G should not capitalize any transaction fees or costs related to the acquisition since the loans are recognized at fair value through earnings. Instead, G should apply the effective-yield guidance in ASC 310-30 and ASC 310-20 on the basis of a net investment in the loan portfolio equal to the initial fair value (in this case, the transaction price is fair value on initial recognition). Entity G will need to allocate the transaction price to the portions of the portfolio accounted for under ASC 310-30 and ASC 310-20 so that it can appropriately apply the applicable interest recognition guidance to each component.

Example 12-11

Measurement of Interest Income on HFS Mortgage Loans That Are Recognized at Fair Value Through Earnings

Entity H is a financial institution that originates and purchases conforming mortgage loans that are held temporarily until they are sold or securitized. Entity H has elected to account for the mortgage loans at fair value through earnings under the FVO in ASC 825. In accordance with its previously elected accounting policy, H separately presents interest income on these HFS mortgage loans in its income statement. In this example, it is assumed that the collectibility of principal and interest on H’s HFS mortgage loans is not in question.

On the basis of these facts, H would measure interest income on the HFS mortgage loans by using the loan’s stated (coupon) rate without amortizing any original issue (purchase) discounts. Such measurement is consistent with how H would measure interest income if it had recognized the loans at the lower of cost or market in accordance with ASC 948-310.
12.4.1.1.2 Presentation of Fees Received and Costs Incurred That Are Associated With the Origination of Loan Receivables Held for Sale

A bank, savings institution, or similar financial institution (a “banking institution”) often originates a loan receivable as a principal, intending to sell the originated loan. (This practice is particularly common in mortgage banking operations.) In these lending arrangements, when banking institutions do not elect the FVO under ASC 825, they classify the originated loans initially and subsequently as HFS and measure them at the lower of cost or fair value. In accordance with ASC 310-20, when banking institutions do not elect the FVO, they capitalize certain fees charged and costs incurred that are associated with origination into the carrying amount of the loans (referred to hereafter as “loan origination fees and costs”). As a result of such capitalization, the loan origination fees and costs enter into the calculation of the gain or loss upon the sale of the loans. In accordance with generally accepted accounting practices for banking institutions (and in a manner consistent with the reporting requirements of the SEC and banking regulators), the net gain or loss on the sale of loans is classified within a single line item as a component of noninterest income (e.g., “gain on sale of loans, net”).

A banking institution may, however, elect to account for its HFS originated loans at fair value through earnings in accordance with the FVO in ASC 825. Under ASC 820 and ASC 825, up-front fees charged and costs incurred are excluded from the measurement of the fair value of financial assets and liabilities and, therefore, are recognized in earnings as charged or incurred. There is no specific U.S. GAAP guidance on how loan origination fees and costs should be classified in the income statement when the FVO is elected for the related loans. Nevertheless, in accordance with generally accepted accounting practices for banking institutions that account for HFS loans at the lower of cost or fair value, the loan origination fees and costs, which are recognized immediately in earnings as charged or incurred, should not be classified within interest income or interest expense. However, there is diversity in practice related to the classification within noninterest income and noninterest expense of loan origination fees and costs related to HFS loans for which the FVO in ASC 825 has been elected.

Given the lack of specific guidance on this topic, either of the following two alternatives is considered acceptable as an accounting policy that should be consistently applied and disclosed if considered significant in accordance with ASC 235-10-50-1:

- **Alternative A: Net-basis classification within noninterest income** — Proponents of this view believe that the income statement classification of loan origination fees and costs should not be affected by whether the banking institution has elected to account for the related HFS loans at fair value through earnings under ASC 825. Rather, such loan origination fees and costs should be classified, and should have an income statement caption, as if the amounts had been capitalized and deferred under ASC 310-20 (i.e., on a net basis within a single line item that is a component of noninterest income). Proponents of this view note that a similar view applies to the classification of interest income and interest expense on loans for which the FVO in ASC 825 has been elected. This approach permits consistent classification regardless of whether the FVO in ASC 825 has been elected, thereby promoting comparability.

- **Alternative B: Gross-basis classification within noninterest income and noninterest expense** — Proponents of this view believe that, in the absence of specific guidance that permits net presentation, the loan origination fees and costs related to HFS loans accounted for at fair value through earnings under the FVO in ASC 825 should be classified on a gross basis. The fees associated with loan origination would be classified as a component of noninterest income, and

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9 Banking institutions may use a different title for this line item (e.g., amounts related to mortgage loans may be presented as a line item titled “mortgage banking income”).

10 ASC 310-20 requires entities to defer loan origination fees and direct loan origination costs (see ASC 310-20-25-2). However, ASC 310-20-15-3 explicitly states that ASC 310-20 does not apply to “[n]onrefundable fees and costs associated with originating or acquiring loans that are carried at fair value if the changes in fair value are included in earnings of a business entity or change in net assets of a not-for-profit entity.”
the costs would be classified as a component of noninterest expense. This view is consistent with the outcome that would result from the application of principal-agent considerations.

Note that the above alternatives apply only when all of the following conditions are met:

- The banking institution prepares an income statement that includes separate totals for interest income, interest expense, noninterest income, and noninterest expense.\(^{11}\)
- The loans are originated for sale (i.e., the loans are HFS loans).
- If the FVO had not been elected, the fees charged and costs incurred would have been capitalized into the carrying amount of the loans in accordance with ASC 310-20.
- The banking institution is acting as a principal in the origination of the loans.\(^{12}\)

### 12.4.1.2 Financial Liabilities for Which FVO is Elected

#### 12.4.1.2.1 Overall Guidance

<table>
<thead>
<tr>
<th>ASC 825-10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Financial Liabilities for Which Fair Value Option Is Elected</strong></td>
</tr>
<tr>
<td><strong>45-5</strong> If an entity has designated a financial liability under the fair value option in accordance with this Subtopic or Subtopic 815-15 on embedded derivatives, the entity shall measure the financial liability at fair value with qualifying changes in fair value recognized in net income. The entity shall present separately in other comprehensive income the portion of the total change in the fair value of the liability that results from a change in the instrument-specific credit risk. The entity may consider the portion of the total change in fair value that excludes the amount resulting from a change in a base market risk, such as a risk-free rate or a benchmark interest rate, to be the result of a change in instrument-specific credit risk. Alternatively, an entity may use another method that it considers to faithfully represent the portion of the total change in fair value resulting from a change in instrument-specific credit risk. The entity shall apply the method consistently to each financial liability from period to period.</td>
</tr>
<tr>
<td><strong>45-5A</strong> When changes in instrument-specific credit risk are presented separately from other changes in fair value of a liability denominated in a currency other than an entity's functional currency, the component of the change in fair value of the liability resulting from changes in instrument-specific credit risk shall first be measured in the liability's currency of denomination, and then the cumulative amount shall be adjusted to reflect the current exchange rate in accordance with paragraph 830-20-35-2. The remeasurement of the component of the change in fair value of the liability resulting from the cumulative changes in instrument-specific credit risk shall be presented in accumulated other comprehensive income.</td>
</tr>
<tr>
<td><strong>45-6</strong> Upon derecognition of a financial liability designated under the fair value option in accordance with this Subtopic, an entity shall include in net income the cumulative amount of the gain or loss on the financial liability that resulted from changes in instrument-specific credit risk.</td>
</tr>
<tr>
<td><strong>45-7</strong> The guidance in paragraph 825-10-45-5 does not apply to financial liabilities of a consolidated collateralized financing entity measured using the measurement alternative in paragraphs 810-10-30-10 through 30-15 and 810-10-35-6 through 35-8.</td>
</tr>
</tbody>
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\(^{11}\) Regulation S-X, Article 9, requires bank holding companies that are SEC registrants to present separate totals for interest income, interest expense, other income, and other expenses. The U.S. banking regulators' call report instructions similarly require that regulated banking institutions present separate totals for interest income, interest expense, non-interest income, and non-interest expense.

\(^{12}\) If the banking institution is merely acting as an agent in the origination of a loan, it would generally be required to report fees and costs associated with the origination of a loan on a net basis.
ASC 815-15

45-2 If an entity has designated a financial liability under the fair value election in accordance with paragraphs 815-15-25-4 through 25-6, the entity shall apply the guidance in paragraph 825-10-45-5 on the presentation of changes in the liability's fair value that result from changes in instrument-specific credit risk.

ASC 830-20

Financial Liabilities for Which the Fair Value Option Is Elected

35-7A Paragraph 825-10-45-5A requires that for a financial liability for which the fair value option is elected, the change in the liability's fair value resulting from changes in instrument-specific credit risk shall be presented separately in other comprehensive income from other changes in the liability's fair value presented in current earnings. The component of the change in fair value of the liability resulting from changes in instrument-specific credit risk shall first be measured in the liability's currency of denomination, and then the cumulative amount shall be adjusted to reflect the current exchange rate in accordance with paragraph 830-20-35-2. The remeasurement of the component of the change in fair value of the liability resulting from the cumulative changes in instrument-specific credit risk shall be presented in accumulated other comprehensive income.

ASC 470-50

Extinguishments of Debt

40-1 As indicated in paragraph 470-50-15-4, the general guidance for the extinguishment of liabilities is contained in Subtopic 405-20 and defines transactions that the debtor shall recognize as an extinguishment of a liability.

40-2 A difference between the reacquisition price of debt and the net carrying amount of the extinguished debt shall be recognized currently in income of the period of extinguishment as losses or gains and identified as a separate item. Gains and losses shall not be amortized to future periods. If upon extinguishment of debt the parties also exchange unstated (or stated) rights or privileges, the portion of the consideration exchanged allocable to such unstated (or stated) rights or privileges shall be given appropriate accounting recognition. Moreover, extinguishment transactions between related entities may be in essence capital transactions.

Pending Content (Transition Guidance: ASC 105-10-65-5)

40-2A In an early extinguishment of debt for which the fair value option has been elected in accordance with Subtopic 815-15 on embedded derivatives or Subtopic 825-10 on financial instruments, the net carrying amount of the extinguished debt shall be equal to its fair value at the reacquisition date. In accordance with paragraph 825-10-45-6, upon extinguishment an entity shall include in net income the cumulative amount of the gain or loss previously recorded in other comprehensive income for the extinguished debt that resulted from changes in instrument-specific credit risk.

ASC 825-10-45-5 requires an entity that has elected to measure a financial liability at fair value in accordance with the FVO to separately present in OCI the portion of the total change in fair value of the liability that is attributable to the change in instrument-specific credit risk, but only if the financial liability contains an instrument-specific credit risk component (see Section 12.4.1.2.2 for discussion of the scope of this special presentation guidance). An entity must determine the portion of the total change in fair value of the financial liability that is attributable to the instrument-specific credit risk so that it can bifurcate the amounts to properly record the amounts in net income and OCI (see Section 12.4.1.2.3 for discussion of how to determine the amount to be recognized in OCI). Upon derecognition of the financial liability, any amounts accumulated in OCI are recognized in net income (see Section 12.4.1.2.4 for discussion of the accounting upon derecognition).
12.4.1.2.2 Scope of Special Presentation Guidance

12.4.1.2.2.1 Nonrecourse Financial Liabilities

The guidance in ASC 825-10-45-5 and 45-5A that requires separate presentation in OCI of the portion of the change in fair value of a financial liability that is attributable to instrument-specific credit risk does not apply to liabilities that do not contain instrument-specific credit risk. A liability that is nonrecourse to the issuer (i.e., the debtor or the borrower) does not contain instrument-specific credit risk. Therefore, changes in fair value associated with a nonrecourse financial liability designated under the FVO should be recognized entirely in earnings. This view was discussed with the FASB staff, which agreed with the conclusion reached.

It is important for an entity to differentiate between instrument-specific credit risk and asset-specific performance risk when assessing a financial liability whose amounts are payable only upon receipt of cash flows from specified assets (e.g., securitization structures). This distinction is important because, in some circumstances, a financial liability may have little or no instrument-specific credit risk and substantially all the changes in the fair value of the liability may be attributable to asset-specific performance risk. We believe that, in such cases, when the issuer or borrower does not have any obligation to make a payment if the assets to which the obligation is contractually linked fail to perform, changes in the fair value of the liability would be recognized in earnings. For example, an entity that issues a note whose cash flows are contractually linked to an underlying pool of assets (e.g., loans, corporate bonds) would have no obligation to make payments unless amounts are received on the underlying pool of assets. In such circumstances, all changes in fair value would be recognized in earnings.

Depending on how the obligation is structured, there may still be some instrument-specific credit risk when there is also asset-specific performance risk. For example, if amounts received on the underlying pool of assets are not immediately payable to the lender (i.e., there is a timing difference between the receipt of cash flows from the assets and the payment on the obligation), the issuer or borrower will owe amounts to the lender even when the assets have performed. Depending on whether the issuer or borrower is able to use the cash received on the assets for purposes other than to pay its obligation under the financial liability, there may be some residual instrument-specific credit risk, which may sometimes be minimal.

12.4.1.2.2.1.1 Financial Liabilities of CFEs

ASC 825-10-45-7 states that the guidance in ASC 825-10-45-5 on separately presenting in OCI the portion of the change in fair value of a financial liability that is attributable to instrument-specific credit risk does not apply to “financial liabilities of a consolidated [CFE] measured using the measurement alternative in paragraphs 810-10-30-10 through 30-15 and 810-10-35-6 through 35-8.” While ASC 825-10-45-7 does not specifically address how the financial liabilities of a CFE are accounted for when the measurement alternative in ASC 810-10-30-10 through 30-15 and ASC 810-10-35-6 through 35-8 is not applied (i.e., when the financial liabilities are measured at fair value in accordance with ASC 820), the guidance in ASC 825-10-45-5 on separately presenting in OCI the portion of the change in fair value of a financial liability that is attributable to instrument-specific credit risk would also generally not apply in such situations. This conclusion is based on the description of a CFE in the ASC master glossary as an entity that issues “beneficial interests [that] have contractual recourse only to the related assets of the collateralized financing entity and are classified as financial liabilities.” Thus, the only instrument-specific credit risk that could exist in the financial liabilities of a CFE would be the timing difference between the receipt of cash flows from the assets and the payment on the obligations for the beneficial interests, as discussed in Section 12.4.1.2.2.1. However, it would be unlikely that even this instrument-specific credit risk component would exist in CFEs.
12.4.1.2.2 Hybrid Financial Liabilities

As clarified in ASU 2018-03, ASC 825-10-45-5 and ASC 815-15-45-2 indicate that the requirement to separately present in OCI the portion of the change in fair value of a financial liability that is attributable to instrument-specific credit risk should also be applied to hybrid financial liabilities for which the FVO has been elected under ASC 815-15-25-4 through 25-6. Furthermore, on the basis of discussions with the FASB staff, this guidance also applies before adoption of ASU 2018-03.

We believe that the scope of the requirement to separately present in OCI the portion of the change in fair value of a financial liability that is attributable to instrument-specific credit risk also encompasses hybrid nonfinancial liabilities to which fair value accounting is applied under ASC 815-15-30-1(b) and ASC 815-15-35-2. However, no portion of the change in fair value of such nonfinancial hybrid instruments would be recognized in OCI if the instrument does not contain any instrument-specific credit risk.

12.4.1.2.3 Measuring Instrument-Specific Credit Risk

The change in fair value attributable to instrument-specific credit risk of a financial asset or financial liability represents the component of the change in fair value of the financial instrument attributable to changes in the specific credit risk of that instrument (e.g., changes in “credit spread” associated with the instrument). As noted in ASC 825-10-45-5, one acceptable method of isolating the change attributable to instrument-specific credit risk is to calculate the hypothetical change in fair value of the instrument during the period that is attributable to changes in the risk-free or benchmark rate and to calculate the difference between that amount and the total change in fair value.

Alternatively, an entity may use another method that it considers to faithfully represent the portion of the total change in fair value resulting from a change in instrument-specific credit risk. However, the entity must apply that method consistently to each financial instrument from period to period. Although the guidance in ASC 825-10-45-5 applies specifically to financial liabilities, we believe that it is applicable by analogy to loans and other receivables held as assets.

See Example 12-12 for an illustration of the calculation of instrument-specific credit risk on the basis of a calculation of the hypothetical change in fair value of the instrument during the period that is attributable to changes in the risk-free or benchmark rate and a comparison of that change to the total change in fair value of the instrument. As discussed above, an entity is not required to use this method to calculate the change in fair value attributable to instrument-specific credit risk.

Example 12-12

Measurement of Instrument-Specific Credit Risk

On January 1, 20X8, Entity I issues an uncollateralized five-year bond with a par value and fair value of $500 million and an interest rate of 8 percent and elects to record the bond at fair value in accordance with the FVO in ASC 825.

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13 The guidance in this section is also relevant to loans and receivables that have been recognized at fair value by using the FVO in ASC 825 or ASC 815-15 because, as discussed in Section 12.5.2, ASC 825 requires disclosure of “[t]he estimated amount of gains and losses [for the period] that are attributable to changes in the instrument-specific credit risk” when these financial assets are recognized at fair value by using the FVO.

14 This method of computing the component of the total change in fair value that is attributable to instrument-specific credit risk is illustrated in paragraphs B5.7.18 and IE1–IE5 of IFRS 9.
Example 12-12 (continued)

Assume the following:

- Interest is paid annually; the bond has a bullet maturity.
- Three-month LIBOR, a benchmark rate, is 5 percent on January 1, 20X8. As of March 31, 20X8, three-month LIBOR has increased to 5.5 percent. (Although LIBOR is used in this example, the entity could also have selected the U.S. Treasury rate as a benchmark rate.)
- The change in three-month LIBOR is the only relevant change in general market conditions.
- The fair value of the bond as of March 31, 20X8, is $495 million, which indicates an 8.3 percent market rate of interest on the bond.
- Entity I computes the change in fair value that is attributable to instrument-specific credit risk by calculating the portion of the total change in fair value of the instrument during the period that is not attributable to changes in general market conditions.
- For simplicity, it is assumed that (1) there is a flat yield curve, (2) all changes in interest rates result from a parallel shift in the yield curve, and (3) the changes in three-month LIBOR are the only relevant changes in general market conditions. An entity should base its calculations on actual market conditions.

Upon issuance of the bond, the market rate of interest on it is 8 percent. The components of the market rate include (1) the benchmark rate (three-month LIBOR) of 5 percent and (2) 3 percent, which represents the bond's credit risk or “credit spread.” At the end of the period, three-month LIBOR increases to 5.5 percent and there are no other changes in general market conditions that would affect the valuation of the bond.

To determine the change in fair value of the bond attributable to instrument-specific credit risk, I calculates the present value of the remaining contractual cash flows by using an 8.5 percent rate consisting of the benchmark interest rate at the end of the period (5.5 percent) and the initial spread from the benchmark rate upon issuance of the bond (3 percent). The resulting present value of the remaining cash flows discounted at 8.5 percent is $492 million.

The fair value of the bond as of December 31, 20X8, is $495 million. Thus, the portion of the change in fair value of the bond attributable to instrument-specific credit risk during the period is $3 million. In other words, the fair value of the bond decreased by $8 million because of a change in general market conditions (the increase in LIBOR) and increased by $3 million because of the narrowing of the credit spread on the bond. Thus, in accordance with ASC 825-10-45-5, in preparing its financial statements and recognizing the bond at fair value, I would reduce the carrying amount of the bond by $5 million and would recognize a loss in earnings of $8 million and a gain in OCI of $3 million. Note that I is also required to determine instrument-specific credit risk for disclosure purposes.

In the absence of other changes in general market conditions, the change in fair value that is attributable to instrument-specific credit risk in the next period would be based on a comparison of the fair value of the bond at the end of the period with the present value of future cash flows discounted at three-month LIBOR at the end of the period, added to an instrument-specific credit spread of 2.8 percent (8.3% – 5.5%). The 8.3 percent represents the implicit market yield on the bond at the end of the previous period (i.e., the effective yield of the bond, which is based on discounting the remaining cash flows and a fair value of $495 million at the beginning of the period). To determine the credit spread at the end of the previous period, I subtracts the 5.5 percent (the benchmark rate at the end of the previous period).
12.4.1.2.3.1 **Foreign-Denominated Financial Liabilities**

ASC 825-10-45-5A and ASC 830-20-35-7A provide guidance on the measurement of the instrument-specific credit risk component of a foreign-denominated financial liability. In accordance with that guidance, entities are required to apply the following two-step measurement approach:

- Measure the instrument-specific credit risk component of the change in fair value of the liability in the liability's currency of denomination.
- Adjust the cumulative amount of changes in instrument-specific credit risk in the currency of denomination of the liability to the entity's functional currency by using the exchange rate as of the measurement date (i.e., the balance sheet date).

12.4.1.2.4 **Extinguishments of Financial Liabilities Measured at Fair Value**

If a financial liability is repaid at its maturity, there will generally not be any remaining component in AOCI related to the cumulative changes in fair value of the financial liability attributable to instrument-specific credit risk. However, if a financial liability recognized at fair value is extinguished before its stated maturity, there will often be a component in AOCI related to the cumulative changes in fair value of the financial liability attributable to instrument-specific credit risk. ASC 470-50-40-2A states that in an early extinguishment of debt for which the FVO has been elected in accordance with ASC 825 or ASC 815-15, an entity should include in net income the cumulative amount of any gain or loss previously recognized in OCI for the extinguished debt that resulted from changes in instrument-specific credit risk. This guidance, which was issued in ASU 2018-09, has transition provisions (i.e., it is not yet effective for all entities). However, we believe that the accounting specified in ASC 470-50-40-2A was the appropriate interpretation of U.S. GAAP before the clarification made in ASU 2018-09.

12.4.2 **Statement of Financial Position**

12.4.2.1 **General**

<table>
<thead>
<tr>
<th>ASC 825-10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Statement of Financial Position</strong></td>
</tr>
<tr>
<td><strong>45-1A</strong> An entity shall separately present financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) in the statement of financial position or the accompanying notes to the financial statements.</td>
</tr>
<tr>
<td><strong>45-1B</strong> Entities shall report assets and liabilities that are measured at fair value pursuant to the fair value option in this Subtopic in a manner that separates those reported fair values from the carrying amounts of similar assets and liabilities measured using another measurement attribute.</td>
</tr>
<tr>
<td><strong>45-2</strong> To accomplish that, an entity shall either:</td>
</tr>
<tr>
<td>a. Present the aggregate of fair value and non-fair-value amounts in the same line item in the statement of financial position and parenthetically disclose the amount measured at fair value included in the aggregate amount</td>
</tr>
<tr>
<td>b. Present two separate line items to display the fair value and non-fair-value carrying amounts.</td>
</tr>
</tbody>
</table>
ASC 825-10-45-1A requires entities to separately present financial assets and financial liabilities by measurement category (e.g., fair value, amortized cost) and form of financial asset (i.e., securities or loans). Such information may be presented either on the face of the statement of financial position or in the notes to the financial statements. Furthermore, an entity that has measured assets or liabilities at fair value under ASC 825 or ASC 815-15 (including those measured at fair value because the entity is unable to reliably identify and measure an embedded derivative that would otherwise need to be bifurcated) must present those assets and liabilities in the statement of financial position in a manner that separates them from the carrying amounts of similar assets and liabilities that are measured by using an attribute other than fair value. ASC 825 and ASC 815-15 identify two ways to accomplish such presentation.

12.4.2.2 Accrued Interest

In the absence of regulations that require separate presentation of accrued interest, the fair value amount presented in the statement of financial position for an interest-bearing financial asset or financial liability accounted for at fair value through earnings should include any interest earned or incurred but not paid (accrued interest). It would, however, be acceptable for an entity to parenthetically disclose the amount of the fair value measurement that represents accrued interest in the financial statement line item for which the interest-bearing financial asset or financial liability accounted for under the FVO is presented.

If there are regulations that require presentation of accrued interest separately from the related interest-bearing financial asset or financial liability for which the FVO has been elected, an entity must do one of the following to comply with the disclosure requirements in ASC 825:

- Present the aggregate amount of accrued interest, which represents part of the fair value of the asset or liability, in a separate line item in the statement of financial position.
- Parenthetically disclose the amount of the fair value measurement that represents accrued interest in the financial statement line item for which the interest-bearing financial asset or financial liability is presented.

See Section 12.4.1.1.1.2 for discussion of how to measure interest income or interest expense when interest is separately presented in the income statement for an interest-bearing financial asset or financial liability that is recognized at fair value through earnings.
12.4.2.3 Netting Under ASC 210-20

The netting of financial assets and financial liabilities under ASC 210-20 is a presentation issue and is not affected by the measurement base of such assets and liabilities. See Example 12-13 for an illustration.

**Example 12-13**

**Offsetting Repurchase Agreements and Reverse Repurchase Agreements**

Entity J has outstanding repurchase agreements ("repos") and reverse repurchase agreements ("reverse repos") with the same counterparty. The repos and reverse repos meet the conditions for offsetting in ASC 210-20-45-11 and 45-12. Entity J can net the repos and reverse repos in the statement of financial position even if it elects to account for them at fair value under the FVO. Since the repos and reverse repos are carried at fair value, the offsetting is based on the fair value carrying amounts and not on the contractual or par amounts.

Further, assume that J has repos and reverse repos with the same counterparty but that only some of the repos and reverse repos are measured at fair value under the FVO. It would be acceptable to apply ASC 825 to measure the repos and reverse repos by using different measurement attributes, provided that J discloses the reasons for electing the FVO for certain contracts and not others. Under these circumstances, and provided that the criteria for offsetting contracts under ASC 210-20 are met, J could net the fair values for contracts for which the FVO was elected with the amortized cost of contracts for which the FVO was not elected.

12.4.3 Statement of Cash Flows

**ASC 825-10**

**Statement of Cash Flows**

45-3 Entities shall classify cash receipts and cash payments related to items measured at fair value according to their nature and purpose as required by Topic 230.

An entity's election of the FVO for financial assets and liabilities does not affect the cash flow statement classification of receipts and payments associated with such financial assets or financial liabilities. In developing Statement 159, the FASB contemplated requiring that cash receipts and cash payments related to financial assets and financial liabilities for which the FVO has been elected be classified as operating activities; however, the Board ultimately rejected this approach. Paragraph A42 of the Basis for Conclusions of Statement 159 states, in part:

"The Board concluded that the cash receipts and cash payments related to trading securities as well as to financial assets and financial liabilities for which the fair value option has been elected should be classified pursuant to Statement 95 (as amended) based on the nature and purpose for which the related financial assets and financial liabilities were acquired or incurred."

See Deloitte’s *A Roadmap to the Preparation of the Statement of Cash Flows* for further discussion of the classification of cash flows in the statement of cash flows.
12.5 Disclosures

12.5.1 General

<table>
<thead>
<tr>
<th>ASC 825-10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Transactions</strong></td>
</tr>
<tr>
<td><strong>50-9</strong> Generally accepted accounting principles (GAAP) require disclosure of or subsequent measurement at fair value for many classes of financial instruments. Those requirements are not superseded or modified by this Subsection.</td>
</tr>
</tbody>
</table>

| **Fair Value Option** |
| **50-24** The principal objectives of the disclosures required by paragraphs 825-10-50-28 through 50-32 are to facilitate both of the following comparisons: |
| a. Comparisons between entities that choose different measurement attributes for similar assets and liabilities |
| b. Comparisons between assets and liabilities in the financial statements of an entity that selects different measurement attributes for similar assets and liabilities. |

| **50-25** Those disclosure requirements are expected to result in the following: |
| a. Information to enable users of its financial statements to understand management’s reasons for electing or partially electing the fair value option |
| b. Information to enable users to understand how changes in fair values affect earnings for the period |
| c. The same information about certain items (such as equity investments and nonperforming loans) that would have been disclosed if the fair value option had not been elected |
| d. Information to enable users to understand the differences between fair values and contractual cash flows for certain items. |

To meet those objectives, the disclosures described in paragraphs 825-10-50-28 through 50-32 are required for items measured at fair value under the option in this Subtopic and the option in paragraph 815-15-25-4. Those disclosures are not required for securities classified as trading securities under Topic 320, life settlement contracts measured at fair value pursuant to Subtopic 325-30, or servicing rights measured at fair value pursuant to Subtopic 860-50. Those Subtopics include disclosure requirements not affected by this Subtopic.

| **50-26** Entities shall provide the disclosures required by paragraphs 825-10-50-28 through 50-32 in both interim and annual financial statements. |

| **50-27** The disclosure requirements in paragraphs 825-10-50-28 through 50-30 do not eliminate disclosure requirements included in other Subtopics, including other disclosure requirements relating to fair value measurement. Entities are encouraged but are not required to present the disclosures required by this Subtopic in combination with related fair value information required to be disclosed by other Subtopics (for example, the General Subsection of this Section and Topic 820). |

Both ASC 820 and ASC 825 contain fair value disclosure requirements that pertain to (1) items measured at fair value on a recurring or nonrecurring basis and (2) items not measured at fair value but for which fair values are disclosed. The fair value disclosures in ASC 825 consist of two types — general fair value disclosures and incremental disclosures required for items measured at fair value in accordance with the FVO in ASC 825 or ASC 815-15. As discussed in ASC 825-10-50-9 and ASC 825-10-50-27, the disclosure requirements of other U.S. GAAP are not superseded by the incremental disclosure requirements in ASC 825 for items measured at fair value by using the FVO. Thus, for items elected under the FVO, an entity must provide the general fair value disclosures required by ASC 820 and ASC 825 in addition to the incremental disclosures required by ASC 825. See Chapter 11 for more information about the other fair value disclosures required by ASC 820 and ASC 825.
ASC 825-10-50-24 through 50-27 outline the objectives of the disclosure requirements for items measured at fair value in accordance with the FVO in ASC 825 or ASC 815-15. Entities must provide these disclosures in interim and annual financial statements. As noted in ASC 825-10-50-25, these disclosures do not apply to certain items measured at fair value in accordance with other Codification topics. ASC 825-10-50-25 lists examples of such items, including debt securities classified as trading under ASC 320, life settlement contracts measured at fair value under ASC 325-30, and servicing rights measured at fair value under ASC 860-50. In addition, we believe that the FVO disclosure requirements do not apply to equity securities measured at fair value under ASC 321. Entities should look to the disclosure requirements of other Codification topics that permit entities to measure these other items at fair value. See further discussion in Appendix A.

12.5.2 Income Statement Disclosures

**ASC 825-10**

**Required Disclosures for Each Period for Which an Interim or Annual Income Statement Is Presented**

**50-30** For each period for which an income statement is presented, entities shall disclose all of the following about items for which the fair value option has been elected:

- a. For each line item in the statement of financial position, the amounts of gains and losses from fair value changes included in earnings during the period and in which line in the income statement those gains and losses are reported. This Subtopic does not preclude an entity from meeting this requirement by disclosing amounts of gains and losses that include amounts of gains and losses for other items measured at fair value, such as items required to be measured at fair value.

- b. A description of how interest and dividends are measured and where they are reported in the income statement. This Subtopic does not address the methods used for recognizing and measuring the amount of dividend income, interest income, and interest expense for items for which the fair value option has been elected.

- c. For loans and other receivables held as assets, both of the following:
  1. The estimated amount of gains or losses included in earnings during the period attributable to changes in instrument-specific credit risk
  2. How the gains or losses attributable to changes in instrument-specific credit risk were determined.

- d. For liabilities, all of the following about the effects of the instrument-specific credit risk and changes in it:
  1. The amount of change, during the period and cumulatively, of the fair value of the liability that is attributable to changes in the instrument-specific credit risk
  2. How the gains and losses attributable to changes in instrument-specific credit risk were determined.
  3. If a liability is settled during the period, the amount, if any, recognized in other comprehensive income that was recognized in net income at settlement.

For each interim or annual period with an income statement, the disclosures above are required for items accounted for at fair value by using the FVO. See ASC 825-10-55-6 through 55-13 for examples illustrating these disclosures.
12.5.3 Disclosures in the Statement of Financial Position

12.5.3.1 Required Disclosures

**ASC 825-10**

<table>
<thead>
<tr>
<th>Required Disclosures as of Each Date for Which an Interim or Annual Statement of Financial Position Is Presented</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>50-28</strong> As of each date for which a statement of financial position is presented, entities shall disclose all of the following:</td>
</tr>
<tr>
<td>a. Management's reasons for electing a fair value option for each eligible item or group of similar eligible items</td>
</tr>
<tr>
<td>b. If the fair value option is elected for some but not all eligible items within a group of similar eligible items, both of the following:</td>
</tr>
<tr>
<td>1. A description of those similar items and the reasons for partial election</td>
</tr>
<tr>
<td>2. Information to enable users to understand how the group of similar items relates to individual line items on the statement of financial position.</td>
</tr>
<tr>
<td>c. For each line item in the statement of financial position that includes an item or items for which the fair value option has been elected, both of the following:</td>
</tr>
<tr>
<td>1. Information to enable users to understand how each line item in the statement of financial position relates to major classes of assets and liabilities presented in accordance with the fair value disclosure requirements of Topic 820. (Paragraph 825-10-50-11 also requires an entity to relate carrying amounts that are disclosed in accordance with that paragraph to what is reported in the statement of financial position.)</td>
</tr>
<tr>
<td>2. The aggregate carrying amount of items included in each line item in the statement of financial position that are not eligible for the fair value option, if any.</td>
</tr>
<tr>
<td>d. The difference between the aggregate fair value and the aggregate unpaid principal balance of each of the following:</td>
</tr>
<tr>
<td>1. Loans and long-term receivables (other than securities subject to Topic 320) that have contractual principal amounts and for which the fair value option has been elected</td>
</tr>
<tr>
<td>2. Long-term debt instruments that have contractual principal amounts and for which the fair value option has been elected.</td>
</tr>
<tr>
<td>e. For loans held as assets for which the fair value option has been elected, all of the following:</td>
</tr>
<tr>
<td>1. The aggregate fair value of loans that are 90 days or more past due</td>
</tr>
<tr>
<td>2. If the entity's policy is to recognize interest income separately from other changes in fair value, the aggregate fair value of loans in nonaccrual status</td>
</tr>
<tr>
<td>3. The difference between the aggregate fair value and the aggregate unpaid principal balance for loans that are 90 days or more past due, in nonaccrual status, or both.</td>
</tr>
<tr>
<td>f. For investments that would have been accounted for under the equity method if the entity had not chosen to apply the fair value option, the information required by paragraph 323-10-50-3 (excluding the disclosures in paragraph 323-10-50-3(a)(3); (b); and (d)).</td>
</tr>
</tbody>
</table>

| **50-29** The disclosure in paragraph 825-10-50-28(f) applies to investments in common stock, investments in in-substance common stock, and other investments (for example, partnerships and certain limited liability corporations) that both: |
| a. Would otherwise be required to be accounted for under the equity method under other generally accepted accounting principles (GAAP) |
| b. Would be required to satisfy the disclosure requirements of paragraph 323-10-50-3. |

When applying paragraph 825-10-50-28(f), an entity shall apply the guidance from paragraphs 323-10-50-2 and 323-10-50-3(a) and (c). |
For each interim or annual period with a statement of financial position, the disclosures above are required for items accounted for at fair value by using the FVO. See ASC 825-10-55-6 through 55-13 for examples illustrating these disclosures.

12.5.3.2 Investments That Would Have Otherwise Been Accounted for by Using the Equity Method

Note that for investments that would have been accounted for under the equity method if the entity had not elected the FVO, the investor must still disclose the information required by ASC 323-10-50-3 except for that in ASC 323-10-50-3(a)(3), ASC 323-10-50-3(b), and ASC 323-10-50-3(d). Thus, for such investments, the following information must be disclosed in the notes to the financial statements or in separate statements or schedules:

- “The name of each investee and percentage of ownership of common stock” (ASC 323-10-50-3(a)(1)).
- “The accounting policies of the investor with respect to investments in common stock. Disclosure shall include the names of any significant investee entities in which the investor holds 20 percent or more of the voting stock, but the common stock is not accounted for on the equity method, together with the reasons why the equity method is not considered appropriate, and the names of any significant investee corporations in which the investor holds less than 20 percent of the voting stock and the common stock is accounted for on the equity method, together with the reasons why the equity method is considered appropriate” (ASC 323-10-50-3(a)(2)).
- “If investments in common stock of corporate joint ventures or other investments accounted for under the equity method are, in the aggregate, material in relation to the financial position or results of operations of an investor, it may be necessary for summarized information as to assets, liabilities, and results of operations of the investees to be disclosed in the notes or in separate statements, either individually or in groups, as appropriate” (ASC 323-10-50-3(c)).

Further, paragraph 2400.4 of the FRM states, in part, that “the [SEC] staff believes that the significance tests in S-X 3-09 and S-X 4-08(g), with the modifications described in Section 2435, should be used by analogy as presumptive thresholds for when the disclosures in . . . [ASC 323-10-50-3c] should be provided for an equity method investment accounted for using fair value in accordance with . . . [ASC 825].” Section 2435 of the FRM describes in detail the modifications that an entity should make to the significance tests in SEC Regulation S-X, Rules 3-09 and 4-08(g), when applying the disclosure requirements in those rules to equity investments that would have been accounted for by using the equity method if the FVO is not elected.
12.5.4 Other Disclosures

ASC 825-10

Other Required Disclosures

50-31 In annual periods only, an entity shall disclose the methods and significant assumptions used to estimate the fair value of items for which the fair value option has been elected. For required disclosures about the method(s) and significant assumptions used to estimate the fair value of financial instruments, see paragraph 820-10-50-2(bbb) except that an entity is not required to provide the quantitative disclosures about significant unobservable inputs used in fair value measurements categorized within Level 3 of the fair value hierarchy required by that paragraph.

50-32 If an entity elects the fair value option at the time one of the events in paragraph 825-10-25-4(d) through (e) occurs, the entity shall disclose both of the following in financial statements for the period of the election:
   a. Qualitative information about the nature of the event
   b. Quantitative information by line item in the statement of financial position indicating which line items in the income statement include the effect on earnings of initially electing the fair value option for an item.

ASC 825-10-50-31 indicates that ASC 820-10-50-2(bbb) addresses the requirement for entities to provide, only for annual periods, disclosures about “the methods and significant assumptions used to estimate the fair value of items for which the [FVO] has been elected.” However, ASC 825-10-50-31 also contains an exception to this requirement under which an entity does not need to “provide the quantitative disclosures about significant unobservable inputs used in fair value measurements categorized within Level 3 of the fair value hierarchy.” Such quantitative disclosures would, however, be required for items measured at fair value under the FVO that are categorized as Level 3 fair value measurements in accordance with ASC 820-10-50-2(bbb). See Chapter 11 for more information about these disclosures.

ASC 825-10-50-32 contains additional disclosure requirements related to FVO elections that occur after a qualifying event under ASC 825-10-25-4(d) and (e). Those events are discussed in Sections 12.3.2.1 and 12.3.2.2.

12.6 Comparison of U.S. GAAP and IFRS Standards

12.6.1 General

As discussed above, ASC 825 and ASC 815-15 address the FVO under U.S. GAAP. Under IFRS Standards, IFRS 9 is the primary source of guidance on the election of and accounting for the FVO. The FVO under U.S. GAAP is similar to the FVO under IFRS 9. Like U.S. GAAP, IFRS Standards permit election of the FVO for certain financial assets and financial liabilities under specific circumstances. Under both U.S. GAAP and IFRS 9, election of the FVO:

1. May be made at initial recognition.
2. Is generally irrevocable.
3. Causes recognition of changes in fair value in earnings and OCI, as applicable.
4. Requires that up-front fees and costs related to items for which the FVO is elected be recognized in earnings as incurred and not deferred.
The table below summarizes the differences between U.S. GAAP and IFRS Standards with respect to the FVO and is followed by a detailed explanation of each difference.\(^{15}\)

<table>
<thead>
<tr>
<th>Subject</th>
<th>U.S. GAAP</th>
<th>IFRS Standards</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scope and qualifying criteria</td>
<td>Entities may elect the FVO for most financial assets and financial liabilities; the ability to elect the FVO for eligible financial instruments is generally not limited.</td>
<td>Entities may elect the FVO for most financial assets and financial liabilities, but only when qualifying criteria are met.</td>
</tr>
<tr>
<td>Election dates</td>
<td>Entities may elect the FVO at initial recognition of a financial instrument or upon the occurrence of certain specified events (see Section 12.3.2).</td>
<td>Entities may elect the FVO at initial recognition of a financial instrument. For financial instruments that represent credit exposures, the FVO may be elected after initial recognition or while the instrument is unrecognized.</td>
</tr>
<tr>
<td>Presentation of fair value changes of financial liabilities</td>
<td>For financial liabilities for which the FVO has been elected, entities defer fair value changes associated with instrument-specific credit risk through OCI. The balance in accumulated AOCI is released into earnings upon derecognition of the financial liability.</td>
<td>For financial liabilities for which the FVO has been elected, entities defer fair value changes associated with credit risk through OCI unless doing so would create or increase an “accounting mismatch” (i.e., an inconsistency in measurement or recognition). The balance in AOCI is not released into earnings upon derecognition of the financial liability.</td>
</tr>
</tbody>
</table>

12.6.2 Scope and Qualifying Criteria

12.6.2.1 Scope

The items to which the FVO can be applied under U.S. GAAP are similar to those under IFRS 9. In both cases, the FVO can be applied to financial assets and financial liabilities that are not otherwise outside the scope of the guidance. Neither U.S. GAAP nor IFRS 9 permits election of the FVO for (1) an investment in an entity for which consolidation is required, (2) employers’ rights and obligations under employee benefit plans, (3) rights and obligations under leases, and (4) financial instruments classified in shareholders’ equity.

However, because the scope of U.S. GAAP guidance on the FVO differs from that of IFRS 9 in certain respects, election of the FVO is not always permitted for the same items. For example, under U.S. GAAP, an entity is permitted to elect the FVO for certain contracts that are outside the scope of IFRS 9, such as insurance contracts and warranties that are not financial instruments. Furthermore, an entity can apply the FVO to equity method investments under U.S. GAAP. With limited exceptions, equity method investments (referred to as “associates”) are outside the scope of the FVO under IFRS 9.

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\(^{15}\) Differences are based on comparison of authoritative literature under U.S. GAAP and IFRS Standards and do not necessarily include interpretations of such literature.
12.6.2.2 Qualifying Criteria

IFRS 9 requires entities to meet certain qualifying criteria before they can elect the FVO for an otherwise eligible item; there are no such qualifying criteria in U.S. GAAP. IFRS 9 provides separate qualifying criteria for financial assets, financial liabilities, and financial instruments for which an entity manages credit risk by using credit derivatives:

- **Financial assets** — IFRS 9 permits an entity to elect the FVO if it “eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as an ‘accounting mismatch’) that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.”

- **Financial liabilities** — IFRS 9 permits an entity to elect the FVO “when doing so results in more relevant information,” which may occur in either of the following situations:
  - The FVO “eliminates or significantly reduces a measurement or recognition inconsistency . . . that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.”
  - A “group of financial liabilities or financial assets and financial liabilities is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the entity's key management personnel.”

Further, IFRS 9 specifies that if “the host is not an asset” within the standard's scope, an entity may use the FVO for a hybrid contract that contains one or more embedded derivatives unless either of the following conditions is met:

- “[T]he embedded derivative(s) do(es) not significantly modify the cash flows that otherwise would be required by the contract.”
- “[I]t is clear with little or no analysis . . . that separation of the embedded derivative(s) is prohibited, such as a prepayment option embedded in a loan that permits the holder to prepay the loan for approximately its amortised cost.”

Moreover, IFRS 9 permits an entity to elect the FVO for all or part of a financial instrument, even if it is outside the scope of IFRS 9 (e.g., an unrecognized instrument), provided that the following criteria are met:

- The credit risk of the designated financial instrument, or part of the financial instrument, is managed by using a “credit derivative that is measured at fair value through profit or loss.”
- The reference entity associated with the credit derivative matches the entity associated with the financial instrument that gives rise to the credit risk (e.g., a borrower or holder of a loan commitment).
- The financial instrument has the same seniority as the financial instrument that can be delivered to the counterparty associated with the credit derivative in accordance with the terms of IFRS 9.

Under U.S. GAAP, an entity is only permitted to apply the FVO to “an entire instrument and not to only specified risks, specific cash flows, or portions of that instrument.” See further discussion in Section 12.3.1.1.3.
12.6.3 Election Dates

Both U.S. GAAP and IFRS 9 permit the election of the FVO at initial recognition. Unlike the election under IFRS 9, the election under U.S. GAAP can also be made for an existing financial instrument when the instrument becomes subject to the equity method of accounting (e.g., because the investor now has significant influence over the investee). Under U.S. GAAP, the FVO can also be elected upon the occurrence of certain other qualifying events, including remeasurement events. See further discussion in Section 12.3.2.

IFRS 9 also permits the election of the FVO for financial instruments to the extent that a credit derivative is used to manage credit risk, at initial recognition, after initial recognition, or while the financial instrument is unrecognized. There is no similar guidance under U.S. GAAP.

Note that when first adopting IFRS 9, an entity is also permitted, in accordance with certain transitional provisions, to designate financial assets and financial liabilities at fair value through profit or loss as of the date of the standard's initial application. The transition guidance of certain ASUs issued by the FASB may allow one-time FVO elections (see Section 12.3.2.1). In addition, other standards in U.S. GAAP may allow entities to make elections to account for certain items at fair value through earnings after initial recognition and in the absence of a remeasurement event.

12.6.4 Presentation of Fair Value Changes of Financial Liabilities

Under both U.S. GAAP and IFRS Standards, changes in the fair value of a financial asset or financial liability for which the FVO has been elected are recognized in earnings (profit or loss). Further, for qualifying financial liabilities for which the FVO has been elected, both U.S. GAAP and IFRS Standards require that the fair value change associated with the liability's credit risk be recognized in OCI.

However, unlike U.S. GAAP, IFRS 9 contains an exception under which deferral of the credit risk component through OCI is precluded if the deferral would “create or enlarge an accounting mismatch in profit or loss.”

Under U.S. GAAP, upon derecognition of a liability for which fair value changes attributable to the liability's credit risk have been recognized through OCI, the credit risk component must be released through earnings upon derecognition of the financial liability (see Section 12.4.1.2.4). However, under IFRS Standards, an entity is not permitted to subsequently release the AOCI component into earnings (or profit or loss) upon derecognition of the liability.
Appendix A — Fair Value Disclosure Requirements of Other Codification Topics

This appendix addresses fair value or fair-value-related presentation and disclosure requirements from FASB Codification topics other than ASC 820 and ASC 825. In some cases, the entire Codification paragraphs are not excerpted below (i.e., only the fair value or fair-value-related guidance is included). In other cases, additional paragraphs from the Codification are included for context. This appendix should not be considered a substitute for the guidance in the Codification.

A.1 ASC 210, Balance Sheet

<table>
<thead>
<tr>
<th>ASC 210-20</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Offsetting of Derivatives, Repurchase Agreements, and Securities Lending Transactions</strong></td>
</tr>
<tr>
<td>50-3 . . [A]n entity shall disclose at the end of the reporting period the following quantitative information separately for assets and liabilities that are within the scope of paragraph 210-20-50-1:</td>
</tr>
<tr>
<td>a. The gross amounts of those recognized assets and those recognized liabilities</td>
</tr>
<tr>
<td>b. The amounts offset in accordance with the guidance in Sections 210-20-45 and 815-10-45 to determine the net amounts presented in the statement of financial position</td>
</tr>
<tr>
<td>c. The net amounts presented in the statement of financial position</td>
</tr>
<tr>
<td>d. The amounts subject to an enforceable master netting arrangement or similar agreement not otherwise included in (b):</td>
</tr>
<tr>
<td>1. The amounts related to recognized financial instruments and other derivative instruments that either:</td>
</tr>
<tr>
<td>i. Management makes an accounting policy election not to offset.</td>
</tr>
<tr>
<td>ii. Do not meet some or all of the guidance in either Section 210-20-45 or Section 815-10-45.</td>
</tr>
<tr>
<td>2. The amounts related to financial collateral (including cash collateral).</td>
</tr>
<tr>
<td>e. The net amount after deducting the amounts in (d) from the amounts in (c).</td>
</tr>
</tbody>
</table>

**Disclosure of Amounts Subject to an Enforceable Master Netting Arrangement or Similar Agreement Not Otherwise Included in Paragraph 210-20-50-3(b)**

55-12 An entity should also disclose the fair value amounts related to cash or financial instrument collateral received or pledged (see paragraph 210-20-50-3(d)(2)).
A.2 ASC 270, Interim Reporting

<table>
<thead>
<tr>
<th>ASC 270-10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Disclosure of Summarized Interim Financial Data by Publicly Traded Companies</strong></td>
</tr>
<tr>
<td>50-1 Many publicly traded companies report summarized financial information at periodic interim dates in considerably less detail than that provided in annual financial statements. While this information provides more timely information than would result if complete financial statements were issued at the end of each interim period, the timeliness of presentation may be partially offset by a reduction in detail in the information provided. As a result, certain guides as to minimum disclosure are desirable. (It should be recognized that the minimum disclosures of summarized interim financial data required of publicly traded companies do not constitute a fair presentation of financial position and results of operations in conformity with generally accepted accounting principles [GAAP].) If publicly traded companies report summarized financial information at interim dates (including reports on fourth quarters), the following data should be reported, as a minimum: . . .</td>
</tr>
<tr>
<td>k. The information about the use of fair value to measure assets and liabilities recognized in the statement of financial position pursuant to Section 820-10-50 . . .</td>
</tr>
<tr>
<td>m. The information about financial instruments as required by Section 825-10-50 . . .</td>
</tr>
</tbody>
</table>

See Section 11.1.4 for more information about this disclosure requirement.

A.3 ASC 310, Receivables

<table>
<thead>
<tr>
<th>ASC 310-10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Fair Value Disclosures</strong></td>
</tr>
<tr>
<td>50-26 Section 825-10-50 provides guidance on the required disclosure of fair values of certain assets and liabilities. Paragraph 825-10-50-8 explains that, for trade receivables and payables, no disclosure is required under that Subtopic if the trade receivable or payable is due in one year or less.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>ASC 310-30</th>
</tr>
</thead>
<tbody>
<tr>
<td>50-2 In addition to disclosures required by other generally accepted accounting principles (GAAP), for each balance sheet presented, an investor shall disclose the following information about loans within the scope of this Subtopic:</td>
</tr>
<tr>
<td>a. Separately for both those loans that are accounted for as debt securities and those loans that are not accounted for as debt securities, all of the following: . . .</td>
</tr>
<tr>
<td>3. For loans acquired during the period, the contractually required payments receivable, cash flows expected to be collected, and fair value at the acquisition date . . .</td>
</tr>
</tbody>
</table>

**Pending Content (Transition Guidance: ASC 326-10-65-1)**

## A.4 ASC 320, Investments — Debt Securities

### ASC 320-10

#### Balance Sheet Classification

**45-1** An entity shall report its investments in available-for-sale securities and trading securities separately from similar assets that are subsequently measured using another measurement attribute on the face of the statement of financial position. To accomplish that, an entity shall do either of the following:

- **a.** Present the aggregate of those fair value and non-fair-value amounts in the same line item and parenthetically disclose the amount of fair value included in the aggregate amount
- **b.** Present two separate line items to display the fair value and non-fair-value carrying amounts.

Entities also shall refer to the guidance in paragraph 825-10-45-1A on disaggregation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables).

#### Securities Classified as Available for Sale

**50-2** For securities classified as available for sale, all reporting entities shall disclose all of the following by major security type as of each date for which a statement of financial position is presented:

- **a.** Amortized cost basis
  - **aa.** Aggregate fair value . . . .

**50-3** Maturity information may be combined in appropriate groupings. In complying with this requirement, financial institutions (see paragraph 942-320-50-1) shall disclose the fair value and the net carrying amount (if different from fair value) of debt securities on the basis of at least the following four maturity groupings:

- **a.** Within one year
- **b.** After one year through five years
- **c.** After 5 years through 10 years
- **d.** After 10 years.

Securities not due at a single maturity date, such as mortgage-backed securities, may be disclosed separately rather than allocated over several maturity groupings; if allocated, the basis for allocation also shall be disclosed.

#### Securities Classified as Held to Maturity

**50-5** For securities classified as held to maturity, all reporting entities shall disclose all of the following by major security type as of each date for which a statement of financial position is presented:

- **a.** Amortized cost basis
  - **aa.** Aggregate fair value
- **b.** Gross unrecognized holding gains
- **c.** Gross unrecognized holding losses . . .

### Pending Content (Transition Guidance: ASC 825-10-65-5)

**50-5A** A public business entity shall disclose the following information for securities classified as held to maturity, by major security type, as of each date for which a statement of financial position is presented:

- **a.** Aggregate fair value
- **b.** Gross unrecognized holding gains
- **c.** Gross unrecognized holding losses.
ASC 320-10 (continued)

Pending Content (Transition Guidance: ASC 825-10-65-5)

50-5B A financial institution that is a public business entity shall disclose the fair value of the debt securities classified as held to maturity, by major security type, on the basis of at least the following four maturity groupings:
   a. Within 1 year
   b. After 1 year through 5 years
   c. After 5 years through 10 years
   d. After 10 years.

Securities not due at a single maturity date, such as mortgage-backed securities, may be disclosed separately rather than allocated over several maturity groupings; if allocated, the basis for allocation also shall be disclosed.

Impairment of Securities

50-6 For all investments in an unrealized loss position, including those that fall within the scope of Subtopic 325-40, for which other-than-temporary impairments have not been recognized in earnings (including investments for which a portion of an other-than-temporary impairment has been recognized in other comprehensive income), an entity shall disclose all of the following in its interim and annual financial statements:
   a. As of each date for which a statement of financial position is presented, quantitative information, aggregated by category of investment — each major security type that the entity discloses in accordance with this Subtopic — in tabular form:
      1. The aggregate related fair value of investments with unrealized losses
      2. The aggregate amount of unrealized losses (that is, the amount by which amortized cost basis exceeds fair value).

Pending Content (Transition Guidance: ASC 326-10-65-1)


ASU 2019-04 deleted the requirement in ASC 320-10-50-5 under which entities other than public business entities must disclose the fair value of held-to-maturity debt securities.

A.5 ASC 321, Investments — Equity Securities

ASC 321-10

Pending Content (Transition Guidance: ASC 825-10-65-5)

50-2B To the extent that the disclosure requirements in this Subtopic achieve the fair value disclosure requirements described in Section 820-10-50 on disclosing fair value measurement, an entity need not duplicate the related fair value disclosure.
Appendix A — Fair Value Disclosure Requirements of Other Codification Topics

ASC 321-10 (continued)

50-3 An entity that applies the guidance in paragraph 321-10-35-2 for equity securities without readily determinable fair values shall disclose all of the following:
   a. The carrying amount of investments without readily determinable fair values
   b. The amount of impairments and downward adjustments, if any, both annual and cumulative
   c. The amount of upward adjustments, if any, both annual and cumulative
   d. As of the date of the most recent statement of financial position, additional information (in narrative form) that is sufficient to permit financial statement users to understand the quantitative disclosures and the information that the entity considered in reaching the carrying amounts and upward or downward adjustments resulting from observable price changes.

Note that the adjustments referred to in ASC 321-10-50-3(b) and 50-3(c), as well as the narrative disclosure referred to in ASC 321-10-50-3(d), are based on fair value measurements. See Sections 2.3.2.1.2 and 2.3.2.2.3 for more information.

A.6 ASC 325, Investments — Other

ASC 325-30

Statement of Financial Position
45-1 An investor shall report its investments that are remeasured at fair value on the face of the statement of financial position separately from those accounted for under the investment method. To accomplish that separate reporting, an investor shall do either of the following:
   a. Display separate line items on the statement of financial position for the fair value method and investment method carrying amounts
   b. Present the aggregate of those fair value method and investment method carrying amounts and parenthetically disclose the amount of those investments accounted for under the fair value method included in the aggregate amount.

Income Statement
45-3 An investor shall report the investment income from its investments in life settlement contracts that are remeasured at fair value on the face of the income statement separately from the investment income from those accounted for under the investment method. To accomplish that separate reporting, an investor shall do either of the following:
   a. Display separate line items on the income statement for the investment income from the investments in life settlement contracts that are accounted for under the fair value method and investment method
   b. Present the aggregate of the investment income in life settlement contracts and parenthetically disclose the investment income from those investments accounted for under the fair value method that are included in the aggregate amount.

45-4 An investor applying the fair value method shall account for premiums paid and life insurance proceeds received on the same financial reporting line as the changes in fair value are reported.

50-3 The disclosure requirements in this Subsection do not eliminate disclosure requirements included in other Topics, including other disclosure requirements on the use of fair value.

Fair Value Method
50-7 An investor shall disclose the method(s) and significant assumptions used to estimate the fair value of investments in life settlement contracts, including any mortality assumptions.
ASC 325-30 (continued)

50-8 An investor shall disclose all of the following for life settlement contracts accounted for under the fair value method based on remaining life expectancy for each of the first five succeeding years from the date of the statement of financial position and thereafter, as well as in the aggregate:

a. The number of life settlement contracts
b. The carrying value of the life settlement contracts
c. The face value (death benefits) of the life insurance policies underlying the contracts.

50-10 An investor shall disclose both of the following for each reporting period presented in the income statement:

a. The gains or losses recognized during the period on investments sold during the period
b. The unrealized gains or losses recognized during the period on investments that are still held at the date of the statement of financial position.

A.7 ASC 326, Financial Instruments — Credit Losses

ASC 326-30

Pending Content (Transition Guidance: ASC 326-10-65-2)

45-1 An entity shall present available-for-sale debt securities on the statement of financial position at fair value. In addition, an entity shall present parenthetically the amortized cost basis and the allowance for credit losses. If for the purposes of identifying and measuring an impairment the applicable accrued interest is excluded from both the fair value and the amortized cost basis of the available-for-sale debt security, an entity may present separately on the statement of financial position or within another statement of financial position line item the accrued interest receivable balance, net of the allowance for credit losses (if any). An entity that presents the accrued interest receivable balance, net of the allowance for credit losses (if any), within another statement of financial position line item shall apply the disclosure requirements in paragraph 326-30-50-3A.

Pending Content (Transition Guidance: ASC 326-10-65-1)

Available-for-Sale Debt Securities in Unrealized Loss Positions Without an Allowance for Credit Losses

50-4 For available-for-sale debt securities, including those that fall within the scope of Subtopic 325-40 on beneficial interests in securitized financial assets, in an unrealized loss position for which an allowance for credit losses has not been recorded, an entity shall disclose all of the following in its interim and annual financial statements:

a. As of each date for which a statement of financial position is presented, quantitative information, aggregated by category of investment — each major security type that the entity discloses in accordance with this Subtopic — in tabular form:
   1. The aggregate related fair value of investments with unrealized losses
   2. The aggregate amount of unrealized losses (that is, the amount by which amortized cost basis exceeds fair value). . . .
A.8  ASC 350, Intangibles — Goodwill and Other

ASC 350-20

Goodwill Impairment Loss

50-2 For each goodwill impairment loss recognized, all of the following information shall be disclosed in the notes to the financial statements that include the period in which the impairment loss is recognized:

a. A description of the facts and circumstances leading to the impairment
b. The amount of the impairment loss and the method of determining the fair value of the associated reporting unit (whether based on quoted market prices, prices of comparable businesses or nonprofit activities, a present value or other valuation technique, or a combination thereof)

50-3 The quantitative disclosures about significant unobservable inputs used in fair value measurements categorized within Level 3 of the fair value hierarchy required by paragraph 820-10-50-2(bbb) are not required for fair value measurements related to the financial accounting and reporting for goodwill after its initial recognition in a business combination.

Goodwill Impairment Loss

50-6 For each goodwill impairment loss recognized, the following information shall be disclosed in the notes to financial statements that include the period in which the impairment loss is recognized:

a. A description of the facts and circumstances leading to the impairment
b. The amount of the impairment loss and the method for determining fair value

c. The caption in the income statement or statement of activities in which the impairment loss is included
d. The method of allocating the impairment loss to the individual amortizable units of goodwill.

50-7 The quantitative disclosures about significant unobservable inputs used in fair value measurements categorized within Level 3 of the fair value hierarchy required by paragraph 820-10-50-2(bbb) are not required for fair value measurements related to the financial accounting and reporting for goodwill after its initial recognition in a business combination or an acquisition by not-for-profit entity.

ASC 350-30

Disclosures Relating to Impairment Losses

50-3 For each impairment loss recognized related to an intangible asset, all of the following information shall be disclosed in the notes to financial statements that include the period in which the impairment loss is recognized:

a. A description of the impaired intangible asset and the facts and circumstances leading to the impairment
b. The amount of the impairment loss and the method for determining fair value

c. The caption in the income statement or the statement of activities in which the impairment loss is aggregated
d. If applicable, the segment in which the impaired intangible asset is reported under Topic 280.

50-3A A nonpublic entity is not required to disclose the quantitative information about significant unobservable inputs used in fair value measurements categorized within Level 3 of the fair value hierarchy required by paragraph 820-10-50-2(bbb) that relate to the financial accounting and reporting for an indefinite-lived intangible asset after its initial recognition.
### A.9 ASC 360, *Property, Plant, and Equipment*

**ASC 360-10**

**Impairment of Long-Lived Assets Classified as Held and Used**

50-2 All of the following information shall be disclosed in the notes to financial statements that include the period in which an impairment loss is recognized:

- a. A description of the impaired long-lived asset (asset group) and the facts and circumstances leading to the impairment
- b. If not separately presented on the face of the statement, the amount of the impairment loss and the caption in the income statement or the statement of activities that includes that loss
- c. The method or methods for determining fair value (whether based on a quoted market price, prices for similar assets, or another valuation technique)
- d. If applicable, the segment in which the impaired long-lived asset (asset group) is reported under Topic 280.

### A.10 ASC 410, *Asset Retirement and Environmental Obligations*

**ASC 410-20**

50-1 An entity shall disclose all of the following information about its asset retirement obligations:

- a. A general description of the asset retirement obligations and the associated long-lived assets
- b. The fair value of assets that are legally restricted for purposes of settling asset retirement obligations
- c. A reconciliation of the beginning and ending aggregate carrying amount of asset retirement obligations showing separately the changes attributable to the following components, whenever there is a significant change in any of these components during the reporting period:
  1. Liabilities incurred in the current period
  2. Liabilities settled in the current period
  3. Accretion expense
  4. Revisions in estimated cash flows.

50-2 If the fair value of an asset retirement obligation cannot be reasonably estimated, that fact and the reasons therefor shall be disclosed.

### A.11 ASC 420, *Exit or Disposal Cost Obligations*

**ASC 420-10**

50-1 All of the following information shall be disclosed in notes to financial statements that include the period in which an exit or disposal activity is initiated and any subsequent period until the activity is completed:

- e. If a liability for a cost associated with the activity is not recognized because fair value cannot be reasonably estimated, that fact and the reasons why.
A.12  **ASC 460, Guarantees**

**ASC 460-10**

**Effect of the Guarantee Disclosure Requirements on the Disclosure Requirements of Other Topics**

50-5 The disclosures required by this Subsection do not eliminate or affect the following disclosure requirements:

a. The requirements in the General Subsection of Section 825-10-50 that certain entities disclose the fair value of their financial guarantees issued . . .

A.13  **ASC 470, Debt**

**ASC 470-20**

**Own-Share Lending Arrangements Issued in Contemplation ofConvertible Debt Issuance**

50-2A An entity that enters into a share-lending arrangement on its own shares in contemplation of a convertible debt offering or other financing shall disclose all of the following. The disclosures must be made on an annual and interim basis in any period in which a share-lending arrangement is outstanding. . . .

   d. The fair value of the outstanding loaned shares as of the balance sheet date . . .

50-2C In the period in which an entity concludes that it is probable that the counterparty to its share-lending arrangement will default, the entity shall disclose the amount of expense reported in the statement of earnings related to the default. The entity shall disclose in any subsequent period any material changes in the amount of expense as a result of changes in the fair value of the entity's shares or the probable recoveries. If default is probable but has not yet occurred, the entity shall disclose the number of shares related to the share-lending arrangement that will be reflected in basic and diluted earnings per share when the counterparty defaults.

**ASC 470-30**

50-1 The borrower's financial statements shall disclose both of the following:

a. The aggregate amount of participating mortgage obligations at the balance sheet date, with separate disclosure of the aggregate participation liabilities and related debt discounts

b. Terms of the participations by the lender in either the appreciation in the fair value of the mortgaged real estate project or the results of operations of the mortgaged real estate project, or both.

A.14  **ASC 480, Distinguishing Liabilities From Equity**

**ASC 480-10**

50-2 Additionally, for all outstanding financial instruments recognized under the guidance in Section 480-10-25 and for each settlement alternative, issuers shall disclose all of the following:

a. The amount that would be paid, or the number of shares that would be issued and their fair value, determined under the conditions specified in the contract if the settlement were to occur at the reporting date

b. How changes in the fair value of the issuer's equity shares would affect those settlement amounts (for example, “the issuer is obligated to issue an additional X shares or pay an additional Y dollars in cash for each $1 decrease in the fair value of one share”). . . .
A.15 **ASC 505, Equity**

**ASC 505-10**

**Contingently Convertible Securities**

50-8 Additionally, the issuer shall disclose in the notes to financial statements the terms of the transaction, including the excess of the aggregate fair value of the instruments that the holder would receive at conversion over the proceeds received and the period over which the discount is amortized.

A.16 **ASC 715, Compensation — Retirement Benefits**

**ASC 715-20**

**Disclosures by Public Entities**

50-1 An employer that sponsors one or more defined benefit pension plans or one or more defined benefit other postretirement plans shall provide the following information, separately for pension plans and other postretirement benefit plans. Amounts related to the employer's results of operations shall be disclosed for each period for which a statement of income is presented. Amounts related to the employer's statement of financial position shall be disclosed as of the date of each statement of financial position presented. All of the following shall be disclosed: . . .

b. A reconciliation of beginning and ending balances of the fair value of plan assets showing separately, if applicable, the effects during the period attributable to each of the following:
   1. Actual return on plan assets
   2. Foreign currency exchange rate changes (see (a)(5))
   3. Contributions by the employer
   4. Contributions by plan participants
   5. Benefits paid
   6. Business combinations
   7. Divestitures
   8. Settlements. . . .

d. The objectives of the disclosures about postretirement benefit plan assets are to provide users of financial statements with an understanding of:
   1. How investment allocation decisions are made, including the factors that are pertinent to an understanding of investment policies and strategies
   2. The classes of plan assets
   3. The inputs and valuation techniques used to measure the fair value of plan assets
   4. The effect of fair value measurements using significant unobservable inputs (Level 3) on changes in plan assets for the period
   5. Significant concentrations of risk within plan assets.

An employer shall consider those overall objectives in providing the following information about plan assets:

i. A narrative description of investment policies and strategies, including target allocation percentages or range of percentages considering the classes of plan assets disclosed pursuant to (ii) below, as of the latest statement of financial position presented (on a weighted-average basis for employers with more than one plan), and other factors that are pertinent to an understanding of those policies and strategies such as investment goals, risk management practices, permitted and prohibited investments including the use of derivatives, diversification, and the relationship between plan assets and benefit obligations. For investment funds disclosed as classes as described in (ii) below, a description of the significant investment strategies of those funds shall be provided.
ii. The fair value of each class of plan assets as of each date for which a statement of financial position is presented. For additional guidance on determining appropriate classes of plan assets, see paragraph 820-10-50-2B. Examples of classes of assets could include, but are not limited to, the following: cash and cash equivalents; equity securities (segregated by industry type, company size, or investment objective); debt securities issued by national, state, and local governments; corporate debt securities; asset-backed securities; structured debt; derivatives on a gross basis (segregated by type of underlying risk in the contract, for example, interest rate contracts, foreign exchange contracts, equity contracts, commodity contracts, credit contracts, and other contracts); investment funds (segregated by type of fund); and real estate. Those examples are not meant to be all inclusive. An employer should consider the overall objectives in paragraph 715-20-50-1(d)(1) through (5) in determining whether additional classes of plan assets or further disaggregation of classes should be disclosed. If an employer determines the measurement date of plan assets in accordance with paragraph 715-30-35-63A or 715-60-35-123A and the employer contributes assets to the plan between the measurement date and its fiscal year-end, the employer shall not adjust the fair value of each class of plan assets for the effects of the contribution. Instead, the employer shall disclose the amount of the contribution to permit reconciliation of the total fair value of all the classes of plan assets to the ending balance of the fair value of plan assets. For example, the contribution could be disclosed as follows:

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iii. A narrative description of the basis used to determine the overall expected long-term rate-of-return-on-assets assumption, such as the general approach used, the extent to which the overall rate-of-return-on-assets assumption was based on historical returns, the extent to which adjustments were made to those historical returns in order to reflect expectations of future returns, and how those adjustments were determined. The description should consider the classes of assets as described in (ii) above, as appropriate.
iv. Information that enables users of financial statements to assess the inputs and valuation techniques used to develop fair value measurements of plan assets at the reporting date. For fair value measurements using significant unobservable inputs, an employer shall disclose the effect of the measurements on changes in plan assets for the period. To meet those objectives, the employer shall disclose the following information for each class of plan assets disclosed pursuant to (ii) above for each annual period:

01. The level of the fair value hierarchy within which the fair value measurements are categorized in their entirety, segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3). The guidance in paragraphs 820-10-35-37 through 35-37A is applicable. Investments for which fair value is measured using the net asset value per share (or its equivalent) practical expedient in paragraph 820-10-35-59 shall not be categorized within the fair value hierarchy, as noted by paragraph 820-10-35-54B. If an employer determines the measurement date of plan assets in accordance with paragraph 715-30-35-63A or 715-60-35-123A and the employer contributes assets to the plan between the measurement date and its fiscal year-end, the employer shall not adjust the fair value of each class of plan assets for the effects of the contribution. Instead, the employer shall disclose the amount of the contribution to permit reconciliation of the total fair value of all plan assets in the fair value hierarchy to the ending balance of the fair value of plan assets. For example, the contribution could be disclosed as follows:

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02. For fair value measurements of plan assets using significant unobservable inputs (Level 3), a reconciliation from the opening balances to the closing balances, disclosing separately changes during the period attributable to the following:

A. Actual Return on Plan Assets (Component of Net Periodic Postretirement Benefit Cost) or Actual Return on Plan Assets (Component of Net Periodic Pension Cost), separately identifying the amount related to assets still held at the reporting date and the amount related to assets sold during the period

B. Purchases, sales, and settlements, net

C. The amounts of any transfers into or out of Level 3 (for example, transfers due to changes in the observability of significant inputs).

03. Information about the valuation technique(s) and inputs used to measure fair value and a discussion of changes in valuation techniques and inputs, if any, during the period.
Entities (Public and Nonpublic) With Two or More Plans

50-2 The disclosures required by this Subtopic shall be aggregated for all of an employer’s defined benefit pension plans and for all of an employer’s other defined benefit postretirement plans unless disaggregating in groups is considered to provide useful information or is otherwise required by the following paragraph and paragraph 715-20-50-4.

50-3 Disclosures about pension plans with assets in excess of the accumulated benefit obligation generally may be aggregated with disclosures about pension plans with accumulated benefit obligations in excess of assets. The same aggregation is permitted for other postretirement benefit plans. If aggregate disclosures are presented, an employer shall disclose both of the following:

a. The aggregate benefit obligation and aggregate fair value of plan assets for plans with benefit obligations in excess of plan assets as of the measurement date of each statement of financial position presented

b. The aggregate pension accumulated benefit obligation and aggregate fair value of plan assets for pension plans with accumulated benefit obligations in excess of plan assets.

Pending Content (Transition Guidance: ASC 715-20-65-4)

50-3 If aggregate disclosures are presented, an employer shall disclose, as of the date of each statement of financial position presented, both of the following:

a. For pension plans, the projected benefit obligation and fair value of plan assets for plans with projected benefit obligations in excess of plan assets, and the accumulated benefit obligation and fair value of plan assets for plans with accumulated benefit obligations in excess of plan assets

b. For other postretirement benefit plans, the accumulated postretirement benefit obligation and fair value of plan assets for plans with accumulated postretirement benefit obligations in excess of plan assets.

50-4 A U.S. reporting entity may combine disclosures about pension plans or other postretirement benefit plans outside the United States with those for U.S. plans unless the benefit obligations of the plans outside the United States are significant relative to the total benefit obligation and those plans use significantly different assumptions. A foreign reporting entity that prepares financial statements in conformity with U.S. generally accepted accounting principles (GAAP) shall apply the preceding guidance to its domestic and foreign plans.

50-5 A nonpublic entity is not required to disclose the information required by paragraph 715-20-50-1(a) through (c), 715-20-50-1(h), 715-20-50-1(m), and 715-20-50-1(o) through (r). A nonpublic entity that sponsors one or more defined benefit pension plans or one or more other defined benefit postretirement plans shall provide all of the following information, separately for pension plans and other postretirement benefit plans. Amounts related to the employer’s results of operations shall be disclosed for each period for which a statement of income is presented. Amounts related to the employer’s statement of financial position shall be disclosed as of the date of each statement of financial position presented.

a. The benefit obligation, fair value of plan assets, and funded status of the plan.

c. The objectives of the disclosures about postretirement benefit plan assets are to provide users of financial statements with an understanding of:

1. How investment allocation decisions are made, including the factors that are pertinent to an understanding of investment policies and strategies

2. The classes of plan assets

3. The inputs and valuation techniques used to measure the fair value of plan assets
ASC 715-20 (continued)

4. The effect of fair value measurements using significant unobservable inputs (Level 3) on changes in plan assets for the period.

5. Significant concentrations of risk within plan assets.

An employer shall consider those overall objectives in providing the following information about plan assets:

i. A narrative description of investment policies and strategies, including target allocation percentages or range of percentages considering the classes of plan assets disclosed pursuant to (ii) below, as of the latest statement of financial position presented (on a weighted-average basis for employers with more than one plan), and other factors that are pertinent to an understanding of those policies and strategies such as investment goals, risk management practices, permitted and prohibited investments including the use of derivatives, diversification, and the relationship between plan assets and benefit obligations. For investment funds disclosed as classes as described in (ii) below, a description of the significant investment strategies of those funds shall be provided.

ii. The fair value of each class of plan assets as of each date for which a statement of financial position is presented. For additional guidance on determining appropriate classes of plan assets, see paragraph 820-10-50-2B. Examples of classes of assets could include, but are not limited to, the following: cash and cash equivalents; equity securities (segregated by industry type, company size, or investment objective); debt securities issued by national, state, and local governments; corporate debt securities; asset-backed securities; structured debt; derivatives on a gross basis (segregated by type of underlying risk in the contract, for example, interest rate contracts, foreign exchange contracts, equity contracts, commodity contracts, credit contracts, and other contracts); investment funds (segregated by type of fund); and real estate. Those examples are not meant to be all inclusive. An employer should consider the overall objectives in paragraph 715-20-50-5(c) (1) through (5) in determining whether additional classes of plan assets or further disaggregation of classes should be disclosed. If an employer determines the measurement date of plan assets in accordance with paragraph 715-30-35-63A or 715-60-35-123A and the employer contributes assets to the plan between the measurement date and its fiscal year-end, the employer shall not adjust the fair value of each class of plan assets for the effects of the contribution. Instead, the employer shall disclose the amount of the contribution to permit reconciliation of the total fair value of all the classes of plan assets to the ending balance of the fair value of plan assets. For example, the contribution could be disclosed as follows:

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03. Information about the valuation technique(s) and inputs used to measure fair value and a discussion of changes in valuation techniques and inputs, if any, during the period.

Pending Content (Transition Guidance: ASC 715-20-65-4)

Disclosures by Nonpublic Entities

50-5 A nonpublic entity is not required to disclose the information required by paragraph 715-20-50-1(a) through (c), 715-20-50-1(h), 715-20-50-1(o) through (q), and 715-20-50-1(r)(2). A nonpublic entity that sponsors one or more defined benefit pension plans or one or more other defined benefit postretirement plans shall provide all of the following information, separately for pension plans and other postretirement benefit plans. Amounts related to the employer’s results of operations shall be disclosed for each period for which a statement of income is presented. Amounts related to the employer’s statement of financial position shall be disclosed as of the date of each statement of financial position presented.

a. The benefit obligation, fair value of plan assets, and funded status of the plan. . .

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</tr>
<tr>
<td>International companies</td>
<td>32,900</td>
<td>24,000</td>
<td>7,600</td>
<td>1,300</td>
</tr>
<tr>
<td>Mortgage-backed securities</td>
<td>13,335</td>
<td></td>
<td>12,780</td>
<td>555</td>
</tr>
<tr>
<td>Assets at fair value at</td>
<td>$102,205</td>
<td>$75,770</td>
<td>$21,580</td>
<td>$4,855</td>
</tr>
<tr>
<td>measurement date of 1/31/20X5</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contributions after</td>
<td>25,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>measurement date</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total assets reported at 2/3/20X5</td>
<td>$127,205</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

02. For fair value measurements of plan assets using significant unobservable inputs (Level 3), the amounts of purchases and any transfers into or out of Level 3 (for example, transfers due to changes in the observability of significant inputs), disclosed separately.

03. Information about the valuation technique(s) and inputs used to measure fair value and a discussion of changes in valuation techniques and inputs, if any, during the period.
Appendix A — Fair Value Disclosure Requirements of Other Codification Topics

ASC 820-10-50-10 states that “[p]lan assets of a defined benefit pension or other postretirement [benefit] plan that are accounted for in accordance with [ASC] 715 are not subject to the disclosure requirements [of ASC 820]. Instead, the disclosures required in paragraphs 715-20-50-1(d)(iv) and 715-20-50-5(c)(iv) shall apply.” Sponsors with postemployment benefits accounted for under ASC 712 that apply the measurement provisions of ASC 715-30 or ASC 715-60 would also be subject to the disclosure requirements in ASC 715.

ASC 715-20-55-16 through 55-18 contain examples illustrating the fair value disclosure requirements of ASC 715-20.

A.17 ASC 718, Compensation — Stock Compensation

<table>
<thead>
<tr>
<th>ASC 718-40</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>50-1</strong> An employer sponsoring an employee stock ownership plan shall disclose all of the following information about the plan, if applicable: . . .</td>
</tr>
<tr>
<td>e. The fair value of unearned employee stock ownership plan shares at the balance-sheet date for shares accounted for under this Subtopic. (Future tax deductions will be allowed only for the employee stock ownership plan's cost of unearned employee stock ownership plan shares.) This disclosure need not be made for old employee stock ownership plan shares for which the employer does not apply the guidance in this Subtopic.</td>
</tr>
<tr>
<td>f. The existence and nature of any repurchase obligation, including disclosure of the fair value (see paragraph 718-40-30-4) of the shares allocated as of the balance sheet date, which are subject to a repurchase obligation. . . .</td>
</tr>
</tbody>
</table>

A.18 ASC 805, Business Combinations

<table>
<thead>
<tr>
<th>ASC 805-10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Business Combinations Occurring During a Current Reporting Period or After the Reporting Date but Before the Financial Statements Are Issued</strong></td>
</tr>
<tr>
<td><strong>50-2</strong> To meet the objective in the preceding paragraph, the acquirer shall disclose the following information for each business combination that occurs during the reporting period: . . .</td>
</tr>
<tr>
<td>g. In a business combination achieved in stages, all of the following:</td>
</tr>
<tr>
<td>1. The acquisition-date fair value of the equity interest in the acquiree held by the acquirer immediately before the acquisition date</td>
</tr>
<tr>
<td>2. The amount of any gain or loss recognized as a result of remeasuring to fair value the equity interest in the acquiree held by the acquirer immediately before the business combination (see paragraph 805-10-25-10) and the line item in the income statement in which that gain or loss is recognized</td>
</tr>
<tr>
<td>3. The valuation technique(s) used to measure the acquisition-date fair value of the equity interest in the acquiree held by the acquirer immediately before the business combination</td>
</tr>
<tr>
<td>4. Information that enables users of the acquirer's financial statements to assess the inputs used to develop the fair value measurement of the equity interest in the acquiree held by the acquirer immediately before the business combination. . . .</td>
</tr>
</tbody>
</table>
ASC 805-20

Business Combinations Occurring During a Current Reporting Period or After the Reporting Date but Before the Financial Statements Are Issued

50-1 Paragraph 805-10-50-1 identifies one of the objectives of disclosures about a business combination. To meet that objective, the acquirer shall disclose all of the following information for each business combination that occurs during the reporting period: . . .

b. For acquired receivables not subject to the requirements of Subtopic 310-30, all of the following:
   1. The fair value of the receivables
   2. The gross contractual amounts receivable
   3. The best estimate at the acquisition date of the contractual cash flows not expected to be collected.

   The disclosures shall be provided by major class of receivable, such as loans, direct financing leases in accordance with Subtopic 840-30, and any other class of receivables. . . .

d. For contingencies, the following disclosures shall be included in the note that describes the business combination:
   1. For assets and liabilities arising from contingencies recognized at the acquisition date:
      i. The amounts recognized at the acquisition date and the measurement basis applied (that is, at fair value or at an amount recognized in accordance with Topic 450 and Section 450-20-25)
      ii. The nature of the contingencies.

   An acquirer may aggregate disclosures for assets or liabilities arising from contingencies that are similar in nature. . . .

e. For each business combination in which the acquirer holds less than 100 percent of the equity interests in the acquiree at the acquisition date, both of the following:
   1. The fair value of the noncontrolling interest in the acquiree at the acquisition date
   2. The valuation technique(s) and significant inputs used to measure the fair value of the noncontrolling interest.

Pending Content (Transition Guidance: ASC 842-10-65-1)

50-1 Paragraph 805-10-50-1 identifies one of the objectives of disclosures about a business combination. To meet that objective, the acquirer shall disclose all of the following information for each business combination that occurs during the reporting period: . . .

b. For acquired receivables not subject to the requirements of Subtopic 310-30, all of the following:
   1. The fair value of the receivables (unless those receivables arise from sales-type leases or direct financing leases by the lessor for which the acquirer shall disclose the amounts recognized as of the acquisition date)
   2. The gross contractual amounts receivable
   3. The best estimate at the acquisition date of the contractual cash flows not expected to be collected.

   The disclosures shall be provided by major class of receivable, such as loans, net investment in sales-type or direct financing leases in accordance with Subtopic 842-30 on leases — lessor, and any other class of receivables. . . .
Appendix A — Fair Value Disclosure Requirements of Other Codification Topics

ASC 805-20 (continued)

Pending Content (Transition Guidance: ASC 842-10-65-1)

d. For contingencies, the following disclosures shall be included in the note that describes the business combination:
   1. For assets and liabilities arising from contingencies recognized at the acquisition date:
      i. The amounts recognized at the acquisition date and the measurement basis applied (that is, at fair value or at an amount recognized in accordance with Topic 450 and Section 450-20-25)
      ii. The nature of the contingencies.
   An acquirer may aggregate disclosures for assets or liabilities arising from contingencies that are similar in nature.

e. For each business combination in which the acquirer holds less than 100 percent of the equity interests in the acquiree at the acquisition date, both of the following:
   1. The fair value of the noncontrolling interest in the acquiree at the acquisition date
   2. The valuation technique(s) and significant inputs used to measure the fair value of the noncontrolling interest.

ASC 805-30

Business Combinations Occurring During a Current Reporting Period or After the Reporting Date but Before the Financial Statements Are Issued

50-1 Paragraph 805-10-50-1 identifies one of the objectives of disclosures about a business combination. To meet that objective, the acquirer shall disclose all of the following information for each business combination that occurs during the reporting period:

b. The acquisition-date fair value of the total consideration transferred and the acquisition-date fair value of each major class of consideration, such as the following:
   1. Cash
   2. Other tangible or intangible assets, including a business or subsidiary of the acquirer
   3. Liabilities incurred, for example, a liability for contingent consideration
   4. Equity interests of the acquirer, including the number of instruments or interests issued or issuable and the method of determining the fair value of those instruments or interests.

ASC 805-50

50-5 If an acquiree elects the option to apply pushdown accounting in its separate financial statements, it shall disclose information in the period in which the pushdown accounting was applied (or in the current reporting period if the acquiree recognizes adjustments that relate to pushdown accounting) that enables users of financial statements to evaluate the effect of pushdown accounting. To meet this disclosure objective, the acquiree shall consider the disclosure requirements in other Subtopics of Topic 805.

50-6 Information to evaluate the effect of pushdown accounting may include the following:

   c. The acquisition-date fair value of the total consideration transferred by the acquirer.
A.19  **ASC 810, Consolidation**

<table>
<thead>
<tr>
<th>ASC 810-10</th>
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</table>

**Deconsolidation of a Subsidiary**

50-1B In the period that either a subsidiary is deconsolidated or a group of assets is derecognized in accordance with paragraph 810-10-40-3A, the parent shall disclose all of the following:

a. The amount of any gain or loss recognized in accordance with paragraph 810-10-40-5
b. The portion of any gain or loss related to the remeasurement of any retained investment in the former subsidiary or group of assets to its fair value
c. The caption in the income statement in which the gain or loss is recognized unless separately presented on the face of the income statement
d. A description of the valuation technique(s) used to measure the fair value of any direct or indirect retained investment in the former subsidiary or group of assets
e. Information that enables users of the parent’s financial statements to assess the inputs used to develop the fair value in item (d)
f. The nature of continuing involvement with the subsidiary or entity acquiring the group of assets after it has been deconsolidated or derecognized
g. Whether the transaction that resulted in the deconsolidation or derecognition was with a related party
h. Whether the former subsidiary or entity acquiring a group of assets will be a related party after deconsolidation.

**Collateralized Financing Entities**

50-20 A reporting entity that consolidates a collateralized financing entity and measures the financial assets and the financial liabilities using the measurement alternative in paragraphs 810-10-30-10 through 30-15 and 810-10-35-6 through 35-8 shall disclose the information required by Topic 820 on fair value measurement and Topic 825 on financial instruments for the financial assets and the financial liabilities of the consolidated collateralized financing entity.

50-21 For the less observable of the fair value of the financial assets and the fair value of the financial liabilities of the collateralized financing entity that is measured in accordance with the measurement alternative in paragraphs 810-10-30-10 through 30-15 and 810-10-35-6 through 35-8, a reporting entity shall disclose that the amount was measured on the basis of the more observable of the fair value of the financial liabilities and the fair value of the financial assets.

50-22 The disclosures in paragraphs 810-10-50-20 through 50-21 do not apply to the financial assets and the financial liabilities that are incidental to the operations of the collateralized financing entity and have carrying values that approximate fair value.
A.20  ASC 815, Derivatives and Hedging

ASC 815-10

Balance Sheet Netting
45-4 Unless the conditions in paragraph 210-20-45-1 are met, the fair value of derivative instruments in a loss position shall not be offset against the fair value of derivative instruments in a gain position. Similarly, amounts recognized as accrued receivables shall not be offset against amounts recognized as accrued payables unless a right of setoff exists.

Pending Content (Transition Guidance: ASC 105-10-65-5)

45-4 Paragraph superseded by Accounting Standards Update No. 2018-09.

Income Statement Classification
45-8 Except for the guidance in the following paragraph and paragraph 815-10-45-10, this Subtopic does not provide guidance about the classification in the income statement of a derivative instrument's gains or losses, including the adjustment to fair value for a contract that newly meets the definition of a derivative instrument.

Derivative Instruments Held for Trading Purposes
45-9 Gains and losses (realized and unrealized) on all derivative instruments within the scope of this Subtopic shall be shown net when recognized in the income statement, whether or not settled physically, if the derivative instruments are held for trading purposes. On an ongoing basis, reclassifications into and out of trading shall be rare.

Options Granted to Employees
45-10 Subsequent changes in the fair value of an option that was granted to an employee and is subject to this Subtopic shall be included in the determination of net income. (See paragraphs 815-10-55-49 through 55-55 for discussion of such an option.) Changes in fair value of the option award before vesting shall be characterized as compensation expense in the employer's income statement. Changes in fair value of the option award after vesting may be reflected elsewhere in the employer's income statement.

Pending Content (Transition Guidance: ASC 718-10-65-11)

45-10 Subsequent changes in the fair value of an option that was granted to a grantee and is subject to or became subject to this Subtopic shall be included in the determination of net income. (See paragraphs 815-10-55-46 through 55-48A and 815-10-55-54 through 55-55 for discussion of such an option.) Changes in fair value of the option award before vesting shall be characterized as compensation cost in the grantor’s income statement. Changes in fair value of the option award after vesting may be reflected elsewhere in the grantor’s income statement.
## Overall Quantitative Disclosures

### 50-4A
An entity that holds or issues derivative instruments (and nonderivative instruments that are designated and qualify as hedging instruments pursuant to paragraphs 815-20-25-58 and 815-20-25-66) shall disclose all of the following for every annual and interim reporting period for which a statement of financial position and statement of financial performance are presented:

- **a.** The location and fair value amounts of derivative instruments (and such nonderivative instruments) reported in the statement of financial position.
- **b.** The location and amount of the gains and losses on derivative instruments (and such nonderivative instruments) and related hedged items reported in any of the following:
  2. The statement of financial position (for example, gains and losses initially recognized in other comprehensive income).

### Pending Content (Transition Guidance: ASC 815-20-65-3)

#### 50-4A
An entity that holds or issues derivative instruments (and nonderivative instruments that are designated and qualify as hedging instruments pursuant to paragraphs 815-20-25-58 and 815-20-25-66) shall disclose all of the following for every annual and interim reporting period for which a statement of financial position and statement of financial performance are presented:

- **a.** The location and fair value amounts of derivative instruments (and such nonderivative instruments) reported in the statement of financial position.
- **b.** The location and amount of the gains and losses on derivative instruments (and such nonderivative instruments) and related hedged items reported in any of the following:
  2. The statement of financial position (for example, gains and losses initially recognized in other comprehensive income).
- **c.** The total amount of each income and expense line item presented in the statement of financial performance in which the results of fair value or cash flow hedges are recorded.

#### 50-4B
The disclosures required by item (a) in the preceding paragraph shall comply with all of the following:

- **a.** The fair value of derivative instruments (and nonderivative instruments that are designated and qualify as hedging instruments pursuant to paragraphs 815-20-25-58 and 815-20-25-66) shall be presented on a gross basis, even when those instruments are subject to master netting arrangements and qualify for net presentation in the statement of financial position in accordance with Subtopic 210-20.
- **b.** Cash collateral payables and receivables associated with those instruments shall not be added to or netted against the fair value amounts.
- **c.** Fair value amounts shall be presented as separate asset and liability values segregated between each of the following:
  1. Those instruments designated and qualifying as hedging instruments under Subtopic 815-20, presented separately by type of contract (for example, interest rate contracts, foreign exchange contracts, equity contracts, commodity contracts, credit contracts, other contracts, and so forth).
  2. Those instruments not designated as hedging instruments, presented separately by type of contract.
- **d.** The disclosure shall identify the line item(s) in the statement of financial position in which the fair value amounts for these categories of derivative instruments are included.

Amounts required to be reported for nonderivative instruments that are designated and qualify as hedging instruments pursuant to paragraphs 815-20-25-58 and 815-20-25-66 shall be the carrying value of the nonderivative hedging instrument, which includes the adjustment for the foreign currency transaction gain or loss on that instrument.
Appendix A — Fair Value Disclosure Requirements of Other Codification Topics

ASC 815-10 (continued)

50-4C The gains and losses disclosed pursuant to paragraph 815-10-50-4A(b) shall be presented separately for all of the following by type of contract (as discussed in the following paragraph):

a. Derivative instruments designated and qualifying as hedging instruments in fair value hedges and related hedged items designated and qualifying in fair value hedges.

b. The effective portion of gains and losses on derivative instruments (and nonderivative instruments) designated and qualifying in cash flow hedges and net investment hedges that was recognized in other comprehensive income during the current period.

c. The effective portion of gains and losses on derivative instruments (and nonderivative instruments) designated and qualifying in cash flow hedges and net investment hedges recorded in accumulated other comprehensive income during the term of the hedging relationship and reclassified into earnings during the current period.

d. The portion of gains and losses on derivative instruments (and nonderivative instruments) designated and qualifying in cash flow hedges and net investment hedges representing any of the following:
   1. The amount of the hedges’ ineffectiveness
   2. The amount, if any, excluded from the assessment of hedge effectiveness.

e. Derivative instruments not designated or qualifying as hedging instruments under Subtopic 815-20 (see paragraph 815-10-50-4F).

Example 21 (see paragraph 815-10-55-182) illustrates the disclosure of fair value amounts of derivative instruments (and such nonderivative instruments) reported in the statement of financial position.

Pending Content (Transition Guidance: ASC 815-20-65-3)

50-4C For qualifying fair value and cash flow hedges, the gains and losses disclosed pursuant to paragraph 815-10-50-4A(b) shall be presented separately for all of the following by type of contract (as discussed in paragraph 815-10-50-4D) and by income and expense line item (if applicable):

a. Derivative instruments (and nonderivative instruments) designated and qualifying as hedging instruments in fair value hedges and related hedged items designated and qualifying in fair value hedges.

b. The gains and losses on derivative instruments designated and qualifying in cash flow hedges included in the assessment of effectiveness that were recognized in other comprehensive income during the current period.

bb. Amounts excluded from the assessment of effectiveness that were recognized in other comprehensive income during the period for which an amortization approach is applied in accordance with paragraph 815-20-25-83A.

c. The gains and losses on derivative instruments designated and qualifying in cash flow hedges that are included in the assessment of effectiveness and recorded in accumulated other comprehensive income during the term of the hedging relationship and reclassified into earnings during the current period.

d. The portion of gains and losses on derivative instruments designated and qualifying in fair value and cash flow hedges representing the amount, if any, excluded from the assessment of hedge effectiveness that is recognized in earnings. When disclosing this amount, an entity shall disclose separately amounts that are recognized in earnings through an amortization approach in accordance with paragraph 815-20-25-83A and amounts recognized through changes in fair value in earnings in accordance with paragraph 815-20-25-83B. . . .

f. The gains and losses reclassified into earnings as a result of the discontinuance of cash flow hedges because it is probable that the original forecasted transactions will not occur by the end of the originally specified time period or within the additional period of time discussed in paragraphs 815-30-40-4 through 40-5.

g. The amount of net gain or loss recognized in earnings when a hedged firm commitment no longer qualifies as a fair value hedge.
Credit-Risk-Related Contingent Features

**50-4H** An entity that holds or issues derivative instruments (or nonderivative instruments that are designated and qualify as hedging instruments pursuant to paragraphs 815-20-25-58 and 815-20-25-66) shall disclose all of the following for every annual and interim reporting period for which a statement of financial position is presented:

a. The existence and nature of credit-risk-related contingent features
b. The circumstances in which credit-risk-related contingent features could be triggered in derivative instruments (or such nonderivative instruments) that are in a net liability position at the end of the reporting period
c. The aggregate fair value amounts of derivative instruments (or such nonderivative instruments) that contain credit-risk-related contingent features that are in a net liability position at the end of the reporting period
d. The aggregate fair value of assets that are already posted as collateral at the end of the reporting period
e. The aggregate fair value of additional assets that would be required to be posted as collateral if the credit-risk-related contingent features were triggered at the end of the reporting period
f. The aggregate fair value of assets needed to settle the instrument immediately if the credit-risk-related contingent features were triggered at the end of the reporting period.

Amounts required to be reported for nonderivative instruments that are designated and qualify as hedging instruments pursuant to paragraphs 815-20-25-58 and 815-20-25-66 shall be the carrying value of the nonderivative hedging instrument, which includes the adjustment for the foreign currency transaction gain or loss on that instrument. Example 23 (see paragraph 815-10-55-185) illustrates a credit-risk-related contingent feature disclosure.

Credit Derivatives

**50-4K** A seller of credit derivatives shall disclose information about its credit derivatives and hybrid instruments (for example, a credit-linked note) that have embedded credit derivatives to enable users of financial statements to assess their potential effect on its financial position, financial performance, and cash flows. Specifically, for each statement of financial position presented, the seller of a credit derivative shall disclose all of the following information for each credit derivative, or each group of similar credit derivatives, even if the likelihood of the seller's having to make any payments under the credit derivative is remote:

- c. The fair value of the credit derivative as of the date of the statement of financial position . . .

However, the disclosures required by this paragraph do not apply to an embedded derivative feature related to the transfer of credit risk that is only in the form of subordination of one financial instrument to another, as described in paragraph 815-15-15-9.

ASC 815-10-45-5 through 45-7 provide guidance on offsetting fair value amounts for derivative instruments and fair value amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) arising from a derivative instrument (or instruments) recognized at fair value and executed with the same counterparty under a master netting arrangement. One of the conditions for offsetting receivables and payables for cash collateral with derivative instruments is that the cash collateral amounts must be fair value amounts in accordance with the definition of fair value in ASC 820. ASC 815-10-50-8 contains disclosure requirements related to offsetting cash collateral amounts with derivative instruments.

ASC 815-10-55-181 through 55-185 provide examples illustrating the disclosures required by ASC 815-10-50-4A through 50-4H.
Appendix A — Fair Value Disclosure Requirements of Other Codification Topics

**ASC 815-15**

45-1 In each statement of financial position presented, an entity shall report hybrid financial instruments measured at fair value under the election and under the practicability exception in paragraph 815-15-30-1 in a manner that separates those reported fair values from the carrying amounts of assets and liabilities subsequently measured using another measurement attribute on the face of the statement of financial position. To accomplish that separate reporting, an entity may do either of the following:

a. Display separate line items for the fair value and non-fair-value carrying amounts
b. Present the aggregate of the fair value and non-fair-value amounts and parenthetically disclose the amount of fair value included in the aggregate amount.

**Hybrid Instruments That Are Not Separated**

50-1 For those hybrid financial instruments measured at fair value under the election and under the practicability exception in paragraph 815-15-30-1, an entity shall also disclose the information specified in paragraphs 825-10-50-28 through 50-32.

50-2 An entity shall provide information that will allow users to understand the effect of changes in the fair value of hybrid financial instruments measured at fair value under the election and under the practicability exception in paragraph 815-15-30-1 on earnings (or other performance indicators for entities that do not report earnings).

**Embedded Conversion Option That Is No Longer Bifurcated**

50-3 An issuer shall disclose both of the following for the period in which an embedded conversion option previously accounted for as a derivative instrument under this Subtopic no longer meets the separation criteria under this Subtopic:

a. A description of the principal changes causing the embedded conversion option to no longer require bifurcation under this Subtopic
b. The amount of the liability for the conversion option reclassified to stockholders’ equity.

The amount that ASC 815-15-50-3(b) requires entities to disclose will represent the fair value of the conversion option immediately before its reclassification from a liability to stockholders’ equity.

**ASC 815-20**

**Pending Content (Transition Guidance: ASC 815-20-65-3)**

**Income Statement Classification**

45-1A For qualifying fair value and cash flow hedges, an entity shall present both of the following in earnings in the same income statement line item that is used to present the earnings effect of the hedged item:

a. The change in the fair value of the hedging instrument that is included in the assessment of hedge effectiveness
b. Amounts excluded from the assessment of hedge effectiveness in accordance with paragraphs 815-20-25-83A through 25-83B.

See paragraphs 815-20-55-79W through 55-79AD for related implementation guidance.
Changes in the fair value of all contracts classified as assets or liabilities shall be disclosed in the financial statements as long as the contracts remain classified as assets or liabilities.

Some contracts that are classified as assets or liabilities meet the definition of a derivative instrument under the provisions of Subtopic 815-10. The related disclosures that are required by Sections 815-10-50, 815-25-50, 815-30-50, and 815-35-50 also are required for those contracts.

Reclassifications and Related Accounting Policy Disclosures

Contracts within the scope of this Subtopic may be required to be reclassified into (or out of) equity during the life of the instrument (in whole or in part) pursuant to the provisions of paragraphs 815-40-35-8 through 35-13. An issuer shall disclose contract reclassifications (including partial reclassifications), the reason for the reclassification, and the effect on the issuer’s financial statements.

The determination of how to partially reclassify contracts subject to this Subtopic is an accounting policy decision that shall be disclosed pursuant to Topic 235.

The disclosures required by Section 505-10-50 apply to all contracts within the scope of this Subtopic as follows:

d. A contract’s current fair value for each settlement alternative (denominated, as relevant, in monetary amounts or quantities of shares) and how changes in the price of the issuer’s equity instruments affect those settlement amounts (for example, the issuer is obligated to issue an additional X shares or pay an additional Y dollars in cash for each $1 decrease in stock price) shall be disclosed under Section 505-10-50. (For some issuers, a tabular format may provide the most concise and informative presentation of these data.)

A.21 ASC 845, Nonmonetary Transactions

An entity shall disclose the amount of revenue and costs (or gains and losses) associated with inventory exchanges recognized at fair value.
A.22  **ASC 860, Transfers and Servicing**

<table>
<thead>
<tr>
<th>ASC 860-20</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Disclosures for Each Income Statement Presented</strong></td>
</tr>
</tbody>
</table>

**50-3** For each income statement presented, the entity shall disclose all of the following: . . .

b. The characteristics of the transfer including all of the following:
   1. A description of the transferor's continuing involvement with the transferred financial assets
   2. The nature and initial fair value of both of the following:
      i. The asset obtained as proceeds
      ii. The liabilities incurred in the transfer.
   3. The gain or loss from sale of transferred financial assets.

bb. For the initial fair value measurements in item (b)(2), the level within the fair value hierarchy in Topic 820 in which the fair value measurements fall, segregating fair value measurements using each of the following:
   1. Quoted prices in active markets for identical assets or liabilities (Level 1)
   2. Significant other observable inputs (Level 2)
   3. Significant unobservable inputs (Level 3).

c. For the initial fair value measurements in item (b)(2), the key inputs and assumptions used in measuring the fair value of assets obtained and liabilities incurred as a result of the sale that relate to the transferor's continuing involvement, including quantitative information about all of the following:
   1. Discount rates.
   2. Expected prepayments including the expected weighted-average life of prepayable financial assets.
      The weighted-average life of prepayable assets in periods (for example, months or years) can be calculated by multiplying the principal collections expected in each future period by the number of periods until that future period, summing those products, and dividing the sum by the initial principal balance.
   3. Anticipated credit losses, including expected static pool losses.
   If an entity has aggregated transfers during a period in accordance with the guidance beginning in paragraph 860-10-50-5, it may disclose the range of assumptions.

c. For the initial fair value measurements in item (b)(2), the valuation technique(s) used to measure fair value.

d. Cash flows between a transferor and transferee, including all of the following:
   1. Proceeds from new transfers
   2. Proceeds from collections reinvested in revolving-period transfers
   3. Purchases of previously transferred financial assets
   4. Servicing fees
   5. Cash flows received from a transferor's interests.
Disclosures for Each Statement of Financial Position Presented

50-4 For each statement of financial position presented, regardless of when the transfer occurred, an entity shall disclose all of the following: . . .

b. The key inputs and assumptions used in measuring the fair value of assets or liabilities that relate to the transferor's continuing involvement including, at a minimum, but not limited to, quantitative information about all of the following:
   1. Discount rates
   2. Expected prepayments including the expected weighted-average life of prepayable financial assets (see paragraph 860-20-50-3(c)(2))
   3. Anticipated credit losses, including expected static pool losses, if applicable. Expected static pool losses can be calculated by summing the actual and projected future credit losses and dividing the sum by the original balance of the pool of assets.

   If an entity has aggregated transfers during a period in accordance with the guidance beginning in paragraph 860-10-50-5, it may disclose the range of assumptions.

c. For the transferor's interest in the transferred financial assets, a sensitivity analysis or stress test showing the hypothetical effect on the fair value of those interests (including any servicing assets or servicing liabilities) of two or more unfavorable variations from the expected levels for each key assumption that is reported under item (b) of this paragraph independently from any change in another key assumption.

d. A description of the objectives, methodology, and limitations of the sensitivity analysis or stress test. . . .

50-4D To provide an understanding of the nature of the transactions, the transferor's continuing exposure to the transferred financial assets, and the presentation of the components of the transaction in the financial statements, an entity shall disclose the following for outstanding transactions at the reporting date that meet the scope guidance in paragraphs 860-20-50-4A through 50-4B by type of transaction (for example, repurchase agreement, securities lending transaction, and sale and total return swap) (except for those transactions that are excluded from the scope, as described in paragraph 860-20-50-4C): . . .

c. Information about the transferor's ongoing exposure to the economic return on the transferred financial assets:
   1. As of the reporting date, the fair value of assets derecognized by the transferor.
   2. Amounts reported in the statement of financial position arising from the transaction (for example, the carrying value or fair value of forward repurchase agreements or swap contracts). To the extent that those amounts are captured in the derivative disclosures presented in accordance with paragraph 815-10-50-4B, an entity shall provide a cross-reference to the appropriate line item in that disclosure.
   3. A description of the arrangements that result in the transferor retaining substantially all of the exposure to the economic return on the transferred financial assets and the risks related to those arrangements.
Appendix A — Fair Value Disclosure Requirements of Other Codification Topics

**ASC 860-20 (continued)**

**Sales of Loans and Trade Receivables**

**50-5** The aggregate amount of gains or losses on sales of loans or trade receivables (including adjustments to record loans held for sale at the lower of cost or fair value) shall be presented separately in the financial statements or disclosed in the notes to financial statements. See Topic 310 for a full discussion of disclosure requirements for loans and trade receivables.

**Pending Content (Transition Guidance: ASC 326-10-65-1)**

**50-5** The aggregate amount of gains or losses on sales of loans or trade receivables (including adjustments to record loans held for sale at the lower of amortized cost basis or fair value) shall be presented separately in the financial statements or disclosed in the notes to financial statements. See Topic 310 on receivables and Topic 326 on measurement of credit losses for a full discussion of disclosure requirements for loans and trade receivables.

**ASC 860-30**

**50-1A** An entity shall disclose all of the following for collateral: . . .

c. If the entity has accepted collateral that it is permitted by contract or custom to sell or repledge, it shall disclose all the following:

1. The fair value as of the date of each statement of financial position presented of that collateral
2. The fair value as of the date of each statement of financial position presented of the portion of that collateral that it has sold or repledged . . .

**Disclosures for Repurchase Agreements, Securities Lending Transactions, and Repurchase-to-Maturity Transactions**

**50-7** To provide an understanding of the nature and risks of short-term collateralized financing obtained through repurchase agreements, securities lending transactions, and repurchase-to-maturity transactions, that are accounted for as secured borrowings at the reporting date, an entity shall disclose the following information for each interim and annual period about the collateral pledged and the associated risks to which the transferor continues to be exposed after the transfer: . . .

c. A discussion of the potential risks associated with the agreements and related collateral pledged, including obligations arising from a decline in the fair value of the collateral pledged and how those risks are managed.

**ASC 860-50**

**45-1** An entity shall report recognized servicing assets and servicing liabilities that are subsequently measured using the fair value measurement method in a manner that separates those carrying amounts on the face of the statement of financial position from the carrying amounts for separately recognized servicing assets and servicing liabilities that are subsequently measured using the amortization method.
45-2 To accomplish that separate reporting, an entity may do either of the following:

a. Display separate line items for the amounts that are subsequently measured using the fair value measurement method and amounts that are subsequently measured using the amortization method.

b. Present the aggregate of those amounts that are subsequently measured at fair value and those amounts that are subsequently measured using the amortization method (see paragraphs 860-50-35-9 through 35-11) and disclose parenthetically the amount that is subsequently measured at fair value that is included in the aggregate amount.

All Servicing Assets and Servicing Liabilities

50-2 For all servicing assets and servicing liabilities, all of the following shall be disclosed:

a. Management’s basis for determining its classes of servicing assets and servicing liabilities.

b. A description of the risks inherent in servicing assets and servicing liabilities and, if applicable, the instruments used to mitigate the income statement effect of changes in fair value of the servicing assets and servicing liabilities.

c. The amount of contractually specified servicing fees, late fees, and ancillary fees recognized for each period for which results of operations are presented, including a description of where each amount is reported in the statement of income.

d. Quantitative and qualitative information about the assumptions used to estimate fair value (for example, discount rates, anticipated credit losses, and prepayment speeds).

Disclosure of quantitative information about the instruments used to manage the risks inherent in servicing assets and servicing liabilities, including the fair value of those instruments at the beginning and end of the period, is encouraged but not required. An entity that provides such quantitative information is also encouraged, but not required, to disclose quantitative and qualitative information about the assumptions used to estimate the fair value of those instruments. Section 235-10-50 provides guidance on disclosures of accounting policies.

Servicing Assets and Servicing Liabilities Subsequently Measured at Fair Value

50-3 For servicing assets and servicing liabilities subsequently measured at fair value, both of the following shall be disclosed:

a. For each class of servicing assets and servicing liabilities, the activity in the balance of servicing assets and the activity in the balance of servicing liabilities (including a description of where changes in fair value are reported in the statement of income for each period for which results of operations are presented), including, but not limited to, the following:
   1. The beginning and ending balances
   2. Additions through any of the following:
      i. Purchases of servicing assets
      ii. Assumptions of servicing obligations
      iii. Recognition of servicing obligations that result from transfers of financial assets.
   3. Disposals
   4. Changes in fair value during the period resulting from either of the following:
      i. Changes in valuation inputs or assumptions used in the valuation model
      ii. Other changes in fair value and a description of those changes.
   5. Other changes that affect the balance and a description of those changes.

See Example 2 (paragraph 860-50-55-27) for an illustration of the disclosure requirement in paragraph 860-50-50-3(a). . . .
Appendix A — Fair Value Disclosure Requirements of Other Codification Topics

ASC 860-50 (continued)

**Servicing Assets and Servicing Liabilities Subsequently Amortized**

**50-4** For servicing assets and servicing liabilities measured subsequently under the amortization method in paragraph 860-50-35-1(a), all of the following shall be disclosed:

a. For each class of servicing assets and servicing liabilities, the activity in the balance of servicing assets and the activity in the balance of servicing liabilities (including a description of where changes in the carrying amount are reported in the statement of income for each period for which results of operations are presented), including, but not limited to, the following: . . .

5. Application of valuation allowance to adjust carrying value of servicing assets

6. Other-than-temporary impairments

7. Other changes that affect the balance and a description of those changes.

b. For each class of servicing assets and servicing liabilities, the fair value of recognized servicing assets and servicing liabilities at the beginning and end of the period . . .

d. The risk characteristics of the underlying financial assets used to stratify recognized servicing assets for purposes of measuring impairment in accordance with paragraph 860-50-35-9. If the predominant risk characteristics and resulting strataums are changed, that fact and the reasons for those changes shall be included in the disclosures about the risk characteristics of the underlying financial assets used to stratify the recognized servicing assets in accordance with this paragraph.

e. For each period for which results of operations are presented, the activity by class in any valuation allowance for impairment of recognized servicing assets, including all of the following:

1. Beginning and ending balances

2. Aggregate additions charged and recoveries credited to operations

3. Aggregate write-downs charged against the allowance.

**Servicing Assets and Servicing Liabilities for Which Subsequent Measurement at Fair Value Is Elected as of the Beginning of the Fiscal Year**

**50-5** If an entity elects under paragraph 860-50-35-3(d) to subsequently measure a class of servicing assets and servicing liabilities at fair value at the beginning of the fiscal year, the amount of the cumulative-effect adjustment to retained earnings shall be separately disclosed.
A.23 ASC 920, Entertainment — Broadcasters

ASC 920-350

Pending Content (Transition Guidance: ASC 926-20-65-2)

License Agreements for Program Material

50-1 An entity shall disclose its methods of accounting for the rights acquired under a license agreement, including, but not limited to, the following methods:
   a. The method or method(s) used in computing amortization
   b. For impairment, a description of the unit(s) of account used for impairment testing and the method(s) used for determining fair value.

50-4 For impairment amounts recognized for a license agreement that is not included in a film group, the following information shall be disclosed in the notes to financial statements that include the period in which the impairment losses are recognized:
   a. A description of the facts and circumstances leading to the impairment
   b. The amount of impairment losses
   c. The caption in the income statement where the impairment losses are recorded
   d. If applicable, the segment(s) under Topic 280 where the impairment losses are recorded.

A.24 ASC 926, Entertainment — Films

ASC 926-20

Pending Content (Transition Guidance: ASC 926-20-65-2)

50-1A An entity shall disclose its methods of accounting for film costs, including, but not limited to, the following:
   a. The method(s) used in computing amortization
   b. For impairment, a description of the unit(s) of account used for impairment testing and the method(s) used for determining fair value.

50-4C For impairment amounts recognized for films or film groups, an entity shall disclose the following information in the notes to financial statements that include the period in which the impairment is recognized:
   a. A general description of the facts and circumstances leading to the impairment
   b. The aggregate amount of impairment losses
   c. The caption in the income statement where the impairment losses are recorded
   d. If applicable, the segment(s) under Topic 280 where the impairment losses are recorded.
Appendix A — Fair Value Disclosure Requirements of Other Codification Topics

A.25  **ASC 940, Financial Services — Brokers and Dealers**

<table>
<thead>
<tr>
<th>ASC 940-320</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Income Statement</strong></td>
</tr>
<tr>
<td><strong>45-4</strong> The changes in the fair value of fixed-income securities owned that were purchased at a discount or premium is composed of accreted interest income or changes in the fair value of the securities or both. Consideration should be given to reporting these components separately as interest income and trading gains and losses, respectively.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>ASC 940-820</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>50-1</strong> Notes to the financial statements shall disclose all of the following if financial instruments' fair values are measured at lower than quoted prices (see Example in paragraph 820-10-55-52):</td>
</tr>
<tr>
<td>a. Description of the financial instrument</td>
</tr>
<tr>
<td>b. The quoted price of the financial instrument</td>
</tr>
<tr>
<td>c. Fair value reported in the statement of financial condition</td>
</tr>
<tr>
<td>d. Methods and significant assumptions used to value the instrument at lower than the quoted price.</td>
</tr>
</tbody>
</table>

A.26  **ASC 942, Financial Services — Depository and Lending**

<table>
<thead>
<tr>
<th>ASC 942-320</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>50-1</strong> For purposes of the disclosure requirements of paragraphs 320-10-50-1 through 50-3 and 320-10-50-5, the term <em>financial institutions</em> includes banks, savings and loan associations, savings banks, credit unions, finance companies, and insurance entities.</td>
</tr>
<tr>
<td><strong>50-1A</strong> The disclosures in paragraphs 942-320-50-1 through 50-3 are required for interim and annual periods.</td>
</tr>
<tr>
<td><strong>50-2</strong> In complying with the requirements in the preceding paragraph, financial institutions shall include in their disclosure all of the following major security types, although additional types also may be necessary:</td>
</tr>
<tr>
<td>a. Equity securities, segregated by any one of the following:</td>
</tr>
<tr>
<td>1. Industry type</td>
</tr>
<tr>
<td>2. Entity size</td>
</tr>
<tr>
<td>3. Investment objective.</td>
</tr>
<tr>
<td>b. Debt securities issued by the U.S. Treasury and other U.S. government corporations and agencies</td>
</tr>
<tr>
<td>c. Debt securities issued by states of the United States and political subdivisions of the states</td>
</tr>
<tr>
<td>d. Debt securities issued by foreign governments</td>
</tr>
<tr>
<td>e. Corporate debt securities</td>
</tr>
<tr>
<td>f. Residential mortgage-backed securities</td>
</tr>
<tr>
<td>ff. Commercial mortgage-backed securities</td>
</tr>
<tr>
<td>fff. Collateralized debt obligations</td>
</tr>
<tr>
<td>g. Other debt obligations.</td>
</tr>
</tbody>
</table>
ASC 942-320 (continued)

50-2A Investments in mutual funds that invest only in U.S. government debt securities may be shown separately rather than grouped with other equity securities in the disclosures by major security type required by paragraph 942-320-50-2.

50-3 In complying with this requirement, financial institutions shall disclose the fair value and the net carrying amount (if different from fair value) of debt securities based on at least 4 maturity groupings:
   a. Within 1 year
   b. After 1 year through 5 years
   c. After 5 years through 10 years
   d. After 10 years.

Pending Content (Transition Guidance: ASC 825-10-65-5)

50-3 In complying with this requirement, financial institutions shall disclose the net carrying amount of debt securities based on at least 4 maturity groupings:
   a. Within 1 year
   b. After 1 year through 5 years
   c. After 5 years through 10 years
   d. After 10 years.

50-3A A financial institution that is a public business entity shall disclose the fair value of the debt securities based on at least 4 maturity groupings:
   a. Within 1 year
   b. After 1 year through 5 years
   c. After 5 years through 10 years
   d. After 10 years.

ASC 942-405

Short Sales of Securities

45-1 The fair value adjustment on short sales of securities shall be classified in the income statement with gains and losses on securities.
A.27 ASC 944, Financial Services — Insurance

ASC 944-40

Pending Content (Transition Guidance: ASC 944-40-65-2)

Market Risk Benefits

45-3 The carrying amount of market risk benefits shall be presented separately in the statement of financial position. The change in fair value related to market risk benefits shall be presented separately in net income, except fair value changes attributable to a change in the instrument-specific credit risk of market risk benefits in a liability position. The portion of a fair value change attributable to a change in the instrument-specific credit risk of market risk benefits in a liability position shall be presented separately in other comprehensive income.

Disclosures

55-13K The tabular rollforward of the beginning to the ending balance related to market risk benefits as required in paragraph 944-40-50-7B could include the following line items:

a. Issuances
b. Interest accrual
c. Attributed fees collected
d. Benefit payments
e. Effect of changes in interest rates
f. Effect of changes in equity markets
g. Effect of changes in equity index volatility
h. Actual policyholder behavior different from expected behavior
i. Effect of changes in future expected policyholder behavior
j. Effect of changes in other future expected assumptions
k. Effect of changes in the instrument-specific credit risk.

To the extent that the tabular rollforward of the beginning to the ending balance related to market risk benefits achieves the fair value disclosure requirements described in Section 820-10-50, an insurance entity need not duplicate the related fair value disclosure.

ASC 944-80

50-1 The following information shall be disclosed in the financial statements of the insurance entity: . . .

e. The aggregate fair value of assets, by major investment asset category, supporting separate accounts with additional insurance benefits and minimum investment return guarantees as of each date for which a statement of financial position is presented . . . .
A.28 **ASC 946, Financial Services — Investment Companies**

**ASC 946-205**

**Separate Accounts**

50-31 Separate accounts with more than two levels of contract charges or net unit values per subaccount may elect to present the required financial highlights for contract expense levels that had units issued or outstanding during the reporting period (including number of units, unit fair value, net assets, expense ratio, investment income ratio, and total return), for either of the following:

a. Each contract expense level that results in a distinct net unit value and for which units were issued or outstanding during each reporting period

b. The range of the lowest and highest level of expense ratio and the related total return and unit fair values during each reporting period.

The calculation of the ranges for the total return ratio and unit fair values should correspond to the groupings that produced the lowest and highest expense ratios.

50-33 If the ranges of expense ratios, total returns, and unit fair values are presented, the entity should disclose instances in which individual contract values do not fall within the ranges presented (for example, if a new product is introduced late in a reporting period and the total return does not fall within the range).

**ASC 946-210**

**Fully Benefit-Responsive Investment Contracts**

45-14 Under Rule 2a-4 of the Investment Company Act of 1940, current net asset value is computed using the fair value of the investment company's portfolio securities.

45-15 The following line items shall be separately reported on the statement of assets and liabilities with a parenthetical reference that such amounts are being reported at fair value:

a. Investments (including traditional guaranteed investment contracts)

b. Wrapper contracts.

45-16 The statement of assets and liabilities of the fund shall present amounts for all of the following:

a. Total assets

b. Total liabilities

c. Net assets reflecting all investments at fair value

d. Net assets.

Amount (d) represents the amount at which participants can transact with the fund. That amount shall be used also for purposes of preparing the per-share disclosures required by Section 946-205-50 and as the beginning and ending balance in the statement of changes in net assets of the fund. The amount representing the difference between (c) and (d) shall be presented on the face of the statement of assets and liabilities as a single amount, calculated as the sum of the amounts necessary to adjust the portion of net assets attributable to each fully benefit-responsive investment contract from fair value to contract value.
The following information shall be disclosed in the financial statements as part of the schedule of investments, to the extent that schedule is already required under paragraph 946-210-50-1, and shall reconcile to corresponding line items on the statement of assets and liabilities:

a. The fair value of each investment contract, including separate disclosure of both of the following:
   1. The fair value of the wrapper contract
   2. The fair value of each of the corresponding underlying investments, if held by the fund, included in that investment contract.

b. Adjustment from fair value to contract value for each investment contract (if the investment contract is fully benefit-responsive)

c. Major credit ratings of the issuer or wrapper provider for each investment contract.

**Investment Companies Other Than Nonregistered Investment Partnerships**

50-1 In the absence of regulatory requirements, investment companies other than nonregistered investment partnerships shall do all of the following:

a. Disclose the name, number of shares, or principal amount of all of the following:
   1. Each investment (including short sales, written options, futures contracts, forward contracts, and other investment-related liabilities) whose fair value constitutes more than 1 percent of net assets.
      In applying the 1-percent test, total long and total short positions in any one issuer should be considered separately.
   2. All investments in any one issuer whose fair values aggregate more than 1 percent of net assets.
      In applying the 1-percent test, total long and total short positions in any one issuer should be considered separately.
   3. At a minimum, the 50 largest investments.

b. Categorize investments by both of the following characteristics:
   1. The type of investment (such as common stocks, preferred stocks, convertible securities, fixed income securities, government securities, options purchased, options written, warrants, futures contracts, loan participations and assignments, short-term securities, repurchase agreements, short sales, forward contracts, other investment companies, and so forth)
   2. The related industry, country, or geographic region of the investment.
ASC 946-210 (continued)

**Investment Companies That Are Nonregistered Investment Partnerships**

50-6 The financial statements of an investment partnership meeting the condition in paragraph 946-210-50-4 shall, at a minimum, include a condensed schedule of investments in securities owned by the partnership at the close of the most recent period. Such a schedule shall do all of the following:

a. Categorize investments by all of the following:
   1. Type (such as common stocks, preferred stocks, convertible securities, fixed-income securities, government securities, options purchased, options written, warrants, futures, loan participations, short sales, other investment companies, and so forth)
   2. Country or geographic region, except for derivative instruments for which the underlying is not a security (see (a)(4))
   3. Industry, except for derivative instruments for which the underlying is not a security (see (a)(4))
   4. For derivative instruments for which the underlying is not a security, by broad category of underlying (for example, grains and feeds, fibers and textiles, foreign currency, or equity indexes) in place of the categories in (a)(2) and (a)(3).

b. Report the percent of net assets that each such category represents and the total fair value and cost for each category in (a)(1) and (a)(2).

c. Disclose the name, number of shares or principal amount, fair value, and type of both of the following:
   1. Each investment (including short sales) constituting more than 5 percent of net assets, except for derivative instruments (see (e) and (f)). In applying the 5-percent test, total long and total short positions in any one issuer should be considered separately.
   2. All investments in any one issuer aggregating more than 5 percent of net assets, except for derivative instruments (see (e) and (f)). In applying the 5-percent test, total long and total short positions in any one issuer shall be considered separately.

d. Aggregate other investments (each of which is 5 percent or less of net assets) without specifically identifying the issuers of such investments, and categorize them in accordance with the guidance in (a). In applying the 5-percent test, total long and total short positions in any one issuer shall be considered separately.

e. Disclose the number of contracts, range of expiration dates, and cumulative appreciation (depreciation) for open futures contracts of a particular underlying (such as wheat, cotton, specified equity index, or U.S. Treasury Bonds), regardless of exchange, delivery location, or delivery date, if cumulative appreciation (depreciation) on the open contracts exceeds 5 percent of net assets. In applying the 5-percent test, total long and total short positions in any one issuer shall be considered separately.

f. Disclose the range of expiration dates and fair value for all other derivative instruments of a particular underlying (such as foreign currency, wheat, specified equity index, or U.S. Treasury Bonds) regardless of counterparty, exchange, or delivery date, if fair value exceeds 5 percent of net assets. In applying the 5-percent test, total long and total short positions in any one issuer shall be considered separately.

g. Provide both of the following additional qualitative descriptions for each investment in another nonregistered investment partnership whose fair value constitutes more than 5 percent of net assets:
   1. The investment objective
   2. Restrictions on redemption (that is, liquidity provisions).
**ASC 946-210 (continued)**

**Fully Benefit-Responsive Investment Contracts**

**50-14** Investment companies identified in paragraph 946-210-45-11 shall disclose all of the following in connection with fully benefit-responsive investment contracts, in the aggregate: . . .

e. A reconciliation between the beginning and ending balance of the amount presented on the statement of assets and liabilities that represents the difference between net assets reflecting all investments at fair value and net assets for each period in which a statement of changes in net assets is presented. This reconciliation shall include both of the following:

1. The change in the difference between the fair value and contract value of all fully benefit-responsive investment contracts
2. The increase or decrease due to changes in the fully benefit-responsive status of the fund's investment contracts.

f. The average yield earned by the entire fund (which may differ from the interest rate credited to participants in the fund) for each period for which a statement of assets and liabilities is presented. This average yield shall be calculated by dividing the annualized earnings of all investments in the fund (irrespective of the interest rate credited to participants in the fund) by the fair value of all investments in the fund. . . .

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**ASC 946-830**

**Overall Guidance**

**45-4** The practice of not separately disclosing the portion of the changes in fair values of investments and realized gains and losses thereon that result from foreign currency rate changes is permitted. However, separate reporting of such gains and losses is allowable and, if adopted by the reporting entity, shall conform to the guidance in this Subtopic.

**Subsequently Measuring at Fair Value**

**45-15** A fund investing in foreign securities generally invests in such securities to reap the potential benefits offered by the local capital market. It may also invest in such securities as a means of investing in the foreign currency market or of benefiting from the foreign currency rate fluctuation. The extent to which separate information regarding foreign currency gains or losses will be meaningful will vary depending on the circumstances, and separate information may not measure with precision foreign exchange gains or losses associated with the economic risks of foreign currency exposures. A foreign currency rate fluctuation, however, may be an important consideration in the case of foreign investments, and a reporting entity may choose to identify and separately report any resulting foreign currency gains or losses as a component of unrealized fair value gains or losses on investments.

**45-16** The fair value of securities shall initially be determined in the foreign currency and translated at the spot rate on the purchase trade date. The unrealized gain or loss between the original cost (translated on the trade date) and the fair value (translated on the valuation date) comprises both of the following elements:

a. Changes in the fair value of securities before translation
b. Movement in foreign currency rate.
ASC 946-830 (continued)

45-17 Such movements may be combined as permitted by paragraph 946-830-45-4. If separate disclosure of the foreign currency gains and losses is chosen, the changes in the fair value of securities before translation should be measured as the difference between the fair value in foreign currency and the original cost in foreign currency translated at the spot rate on the valuation date. The effect of the movement in the foreign exchange rate shall be measured as the difference between the original cost in foreign currency translated at the current spot rate and the historical functional currency cost. These values can be computed as follows:

a. \((\text{Fair value in foreign currency} - \text{original cost in foreign currency}) \times \text{valuation date spot rate} = \text{unrealized fair value appreciation or depreciation.}\)

b. \((\text{Cost in foreign currency} \times \text{valuation date spot rate}) - \text{cost in functional currency} = \text{the unrealized foreign currency gain or loss.}\)

Sale of Securities

45-20 If separate reporting of foreign currency gains and losses on sales of securities is chosen by the reporting entity, the computation of the effects of the changes in fair value and the foreign currency rate is similar to that described in paragraphs 946-830-45-17 through 45-18. Fair value in the formula given in those paragraphs should be replaced with sale proceeds and valuation date shall be replaced with sale trade date. Accordingly, the values shall be computed as follows:

a. \((\text{Sale proceeds in foreign currency} - \text{original cost in foreign currency}) \times \text{sale trade date spot rate} = \text{realized fair value gain or loss on sale of security.}\)

b. \((\text{Cost in foreign currency} \times \text{sale trade date spot rate}) - \text{cost in functional currency} = \text{realized foreign currency gain or loss.}\)

50-2 Foreign currency risk associated with investing in foreign securities shall be assessed continuously by management and considered for financial statement disclosure, including disclosures about all of the following:

a. Liquidity. Because certain foreign markets are illiquid, market prices may not necessarily represent fair value.

b. Size. If market capitalization is low, a fund's share in the entire market (particularly if single-country funds are involved) or in specific securities may be proportionately very large, and the fair value, consistent with Topic 820, may not be representative of the price that would be received if the fund sold its large proportion of the specific security ("block") at the measurement date.

c. Valuation. Because of liquidity problems as well as other factors, such as securities that are unlisted or securities that are traded in inactive markets, funds are required to develop procedures consistent with Topic 820 for measuring the fair values of such securities. Doing so may be difficult in a foreign environment; while others may perform the research and provide supporting documentation for fair values, the ultimate responsibility for determining the fair values of securities rests with the management.
### A.29 ASC 948, Financial Services — Mortgage Banking

**ASC 948-310**

*50-1* The method used in determining the lower of cost or fair value of mortgage loans (that is, aggregate or individual loan basis) shall be disclosed.

**Pending Content (Transition Guidance: ASC 326-10-65-1)**

*50-1* The method used in determining the lower of amortized cost basis or fair value of mortgage loans (that is, aggregate or individual loan basis) shall be disclosed.

### A.30 ASC 954, Health Care Entities

**ASC 954-220**

**Performance Indicator and Intermediate Operating Measures**

*45-8* Health care entities shall report the following items separately from the performance indicator: . . .

- **e.** Items that are required to be reported in or reclassified from other comprehensive income in accordance with paragraph 220-10-45-10A, which includes, but is not limited to, gains or losses, prior service costs or credits, and transition assets or obligations recognized in accordance with Topic 715; foreign currency translation adjustments; and the effective portion of the gain or loss on derivative instruments designated and qualifying as cash flow hedging instruments. . . .

- **g.** Unrealized gains and losses on investments on other than trading securities, in accordance with paragraph 954-220-45-9. . . .

- **l.** The portion of the total change in the fair value of the liability resulting from a change in the instrument-specific credit risk, in accordance with paragraph 825-10-45-5. . . .

**Pending Content (Transition Guidance: ASC 815-20-65-3)**

**Performance Indicator and Intermediate Operating Measures**

*45-8* Health care entities shall report the following items separately from the performance indicator: . . .

- **e.** Items that are required to be reported in or reclassified from other comprehensive income in accordance with paragraph 220-10-45-10A, which includes, but is not limited to, gains or losses, prior service costs or credits, and transition assets or obligations recognized in accordance with Topic 715; foreign currency translation adjustments; the portion of the gain or loss on derivative instruments designated and qualifying as cash flow hedging instruments included in the assessment of effectiveness, and for all qualifying hedging relationships amounts excluded from the assessment of effectiveness and recognized in earnings through an amortization approach in accordance with paragraph 815-20-25-83A. . . .

- **g.** Unrealized gains and losses on investments on other than trading debt securities, in accordance with paragraph 954-220-45-9. . . .

- **l.** The portion of the total change in the fair value of the liability resulting from a change in the instrument-specific credit risk, in accordance with paragraph 825-10-45-5. . . .
ASC 954-805

35-1 An acquirer that is a not-for-profit, business-oriented health care entity shall report the changes in the fair value of contingent consideration recognized in accordance with paragraph 958-805-35-3 within the performance indicator unless the arrangement is a hedging instrument for which Subtopic 954-815 requires the entity to recognize the changes outside the performance indicator.

ASC 954-825

45-1 Not-for-profit, business-oriented health care entities shall report unrealized gains and losses on items for which the fair value option has been elected within the performance indicator or as a part of discontinued operations, as appropriate. See paragraph 825-10-15-7 for further guidance.

A.31  ASC 958, Not-for-Profit Entities

ASC 958-30

50-1 The notes to financial statements shall include all of the following disclosures related to split-interest agreements: . . .

   c. The basis used (for example, cost, lower of cost or fair value, fair value) for recognized assets . . .
   f. Changes in the value of split-interest agreements recognized, if not reported as a separate line item in a statement of activities
   g. The disclosures required by the Fair Value Option Subsections of Subtopic 825-10, if a not-for-profit entity (NFP) elects the fair value option pursuant to paragraph 958-30-35-2(b) or 958-30-35-2(c)
   h. The disclosures required by paragraphs 820-10-50-1 through 50-2 and 820-10-50-2B through 50-2E in the format described in paragraph 820-10-50-8, if the assets and liabilities of split-interest agreements are measured at fair value on a recurring basis in periods after initial recognition.

Pending Content (Transition Guidance: ASC 820-10-65-12)

50-1 The notes to financial statements shall include all of the following disclosures related to split-interest agreements: . . .

   c. The basis used (for example, cost, lower of cost or fair value, fair value) for recognized assets . . .
   f. Changes in the value of split-interest agreements recognized, if not reported as a separate line item in a statement of activities
   g. The disclosures required by the Fair Value Option Subsections of Subtopic 825-10, if a not-for-profit entity (NFP) elects the fair value option pursuant to paragraph 958-30-35-2(b) or 958-30-35-2(c)
   h. The disclosures required by paragraphs 820-10-50-1C through 50-2 and 820-10-50-2B through 50-2E in the format described in paragraph 820-10-50-8, if the assets and liabilities of split-interest agreements are measured at fair value on a recurring basis in periods after initial recognition.
## ASC 958-205

### Reporting Endowment Funds

50-2 For each period for which a statement of financial position is presented, an NFP shall disclose each of the following, in the aggregate, for all underwater endowment funds:

a. The fair value of the underwater endowment funds
b. The original endowment gift amount or level required to be maintained by donor stipulations or by law that extends donor restrictions
c. The amount of the deficiencies of the underwater endowment funds (a) less (b).

## ASC 958-310

### Accrual of the Interest Element

35-6 If a present value technique is used to measure the fair value of unconditional promises to give cash, subsequent accruals of the interest element pursuant to Section 835-30-35 shall be accounted for as contribution revenue by donees.

### Changes in the Fair Value of Underlying Noncash Assets — Gifts of Other Assets

35-13 If the future fair value of the underlying noncash asset decreases, that decrease shall be reported as a decrease in contribution revenue in the period(s) in which the decrease occurs. The decrease shall be reported in the net asset class in which the contribution was originally reported or in the net asset class in which the net assets are represented. Thus, if a promise to give noncash assets is measured based on the fair value of those underlying noncash assets at the date of gift, as described in paragraph 958-605-30-8, an observed decrease in the current fair value of the underlying noncash asset shall be recognized. If the future fair value of the underlying noncash asset increases between the date the unconditional promise to give is recognized and the date the asset promised is received, no additional revenue shall be recognized.

## ASC 958-321

50-2 The disclosure guidance in Section 321-10-50, except for paragraph 321-10-50-4, applies to investments in equity securities held by NFPs.

## ASC 958-325

50-2 For each period for which a statement of financial position is presented, an NFP shall disclose all of the following:

a. The basis for determining the carrying amount for other investments
b. The method(s) and significant assumptions used to estimate the fair values of investments other than financial instruments if those other investments are reported at fair value . . . .
Accounting Policies

50-1 A not-for-profit entity (NFP) shall disclose the following accounting policies: . . .

   e. The basis of valuation of property, plant, and equipment — for example, cost for purchased items and
      fair value for contributed items.

Works of Art, Historical Treasures, and Similar Assets

50-6 An NFP that does not recognize and capitalize its collections or that capitalizes collections prospectively
shall describe its collections, including their relative significance, and its stewardship policies for collections. If
collection items not capitalized are deaccessioned during the period, it also shall describe the items given away,
damaged, destroyed, lost, or otherwise deaccessed during the period or disclose their fair value.

Contributed Services

50-1 An entity that receives contributed services shall describe the programs or activities for which those
services were used, including the nature and extent of contributed services received for the period and the
amount recognized as revenues for the period. Entities are encouraged to disclose the fair value of contributed
services received but not recognized as revenues if that is practicable. The nature and extent of contributed
services received can be described by nonmonetary information, such as the number and trends of donated
hours received or service outputs provided by volunteer efforts, or other monetary information, such as the
dollar amount of contributions raised by volunteers. Disclosure of contributed services is required regardless
of whether the services received are recognized as revenue in the financial statements.

Instead of the information required by Section 805-30-50, an NFP acquirer shall disclose the following
information for each acquisition that occurs during the reporting period: . . .

   b. The acquisition-date fair value of the total consideration transferred (or if no consideration was
      transferred, that fact) and the acquisition-date fair value of each major class of consideration, such as:
      1. Cash
      2. Other tangible or intangible assets, including a business or subsidiary of the acquirer
      3. Liabilities incurred, for example, a liability for contingent consideration. . . .
A.32  ASC 960, Plan Accounting — Defined Benefit Pension Plans

**ASC 960-30**

**Changes in Net Assets Available for Benefits**

45-2 Information about changes in net assets available for benefits is intended to present the effects of significant changes in net assets during the year and shall present, at a minimum, all of the following:

- a. The net appreciation (depreciation) in fair value. Net appreciation or depreciation includes realized gains and losses on investments that were both purchased and sold during the period as well as unrealized appreciation or depreciation of the investments held at year-end.
- b. Investment income (exclusive of (a)).
- c. Contributions from the employer, segregated between cash and noncash contributions. A noncash contribution shall be recorded at fair value. The nature of noncash contributions shall be described, either parenthetically or in a note.

**Master Trust Investments**

50-1 In the notes to financial statements the investments of a master trust measured using fair value shall be detailed by general type, such as the following, as of the date of each statement of net assets available for benefits presented:

- a. Government securities
- b. Short-term securities
- c. Corporate bonds
- d. Common stocks
- e. Mortgages
- f. Real estate.

---

**Pending Content (Transition Guidance: ASC 962-10-65-4)**

50-1 Paragraph superseded by Accounting Standards Update No. 2017-06.

50-2 The net change in the fair value of investments of the master trust and total investment income of the master trust by type, including interest, dividends, and so forth, also shall be disclosed in the notes for each period for which a statement of changes in net assets available for benefits is presented.

---

**ASC 960-325**

45-1 Information regarding a plan's investments that are measured using fair value shall indicate whether reported fair values have been measured by quoted prices in an active market or are fair values otherwise determined.
**ASC 960-325 (continued)**

45-2 Investments measured using fair value in the statement of net assets available for benefits or in the notes shall be presented by general type, such as the following:

a. Registered investment companies (for example, mutual funds)
b. Government securities
c. Common-collective trusts
d. Pooled separate accounts
e. Short-term securities
f. Corporate bonds
g. Common stocks
h. Mortgages
i. Real estate.

50-1 Disclosure of the plan's accounting policies shall include a description of valuation techniques and inputs used to measure the fair value of investments (as required by Section 820-10-50) and a description of the methods and significant assumptions used to measure the reported value of contracts with insurance entities. However, defined benefit pension plans are exempt from the requirements in paragraph 820-10-50-2B(a) to disaggregate assets by nature, characteristics, and risks. The disclosures of information by classes of assets required by Section 820-10-50 shall be provided by general type of plan assets consistent with paragraph 960-325-45-2.

50-3 The historical cost of plan investments presented at fair value is neither required nor proscribed.

**Pending Content (Transition Guidance: ASC 962-10-65-4)**

**Interests in Master Trusts**

50-7 A plan shall disclose the following in the notes to financial statements for each period for which a statement of changes in net assets available for benefits is presented:

a. Net appreciation or depreciation in the fair value of investments of the master trust. Net appreciation or depreciation includes realized gains and losses on investments that were both purchased and sold during the period as well as unrealized appreciation or depreciation of the investments held at year-end.
b. Investment income (exclusive of (a)).

50-9 In the notes to financial statements a plan shall include the investments of a master trust measured using fair value presented by general type of investment, such as the following, as of the date of each statement of net assets available for benefits presented:

a. Registered investment companies (for example, mutual funds)
b. Government securities
c. Common-collective trusts
d. Pooled separate accounts
e. Short-term securities
f. Corporate bonds
g. Common stocks
h. Mortgages
i. Real estate.
Appendix A — Fair Value Disclosure Requirements of Other Codification Topics

**A.33 ASC 962, Plan Accounting — Defined Contribution Pension Plans**

<table>
<thead>
<tr>
<th>ASC 962-205</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Changes in Net Assets Available for Benefits</strong></td>
</tr>
<tr>
<td><strong>45-7</strong> Information about changes in net assets available for benefits is intended to present the effects of significant changes in net assets during the year and shall present, at a minimum, all of the following:</td>
</tr>
<tr>
<td>a. The net appreciation or depreciation in fair value. Net appreciation or depreciation includes realized gains and losses on investments that were both purchased and sold during the period as well as unrealized appreciation or depreciation of the investments held at year end.</td>
</tr>
<tr>
<td>b. Investment income, exclusive of changes in fair value described in (a). . . .</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>ASC 962-310</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Participant Loans</strong></td>
</tr>
<tr>
<td><strong>50-1</strong> The fair value disclosures prescribed in paragraphs 825-10-50-10 through 50-16 are not required for participant loans.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>ASC 962-325</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>45-5</strong> Investments measured using fair value in the statement of net assets available for benefits or in the notes shall be presented by general type, such as the following:</td>
</tr>
<tr>
<td>a. Registered investment companies (for example, mutual funds)</td>
</tr>
<tr>
<td>b. Government securities</td>
</tr>
<tr>
<td>c. Common-collective trusts</td>
</tr>
<tr>
<td>d. Pooled separate accounts</td>
</tr>
<tr>
<td>e. Short-term securities</td>
</tr>
<tr>
<td>f. Corporate bonds</td>
</tr>
<tr>
<td>g. Common stocks</td>
</tr>
<tr>
<td>h. Mortgages . . .</td>
</tr>
<tr>
<td>j. Real estate</td>
</tr>
<tr>
<td>k. Self-directed brokerage accounts (that is, an investment option that allows participants to select investments outside the plan’s core options).</td>
</tr>
</tbody>
</table>

For the presentation of fully benefit-responsive investment contracts, which are measured at contract value, see paragraphs 962-325-35-5A and 962-325-50-3.

**45-6** The presentation shall indicate whether the fair values of the investments have been measured by quoted market prices in an active market or were determined otherwise.

**50-1** Disclosure of a defined contribution plan’s accounting policies shall include a description of the valuation techniques and inputs used to measure the fair value less costs to sell, if significant, of investments (as required by Section 820-10-50) and a description of the methods and significant assumptions used to measure the reported value of insurance contracts (if any). . . .
ASC 962-325 (continued)

Master Trust Investments

50-6 In the notes to financial statements the investments of a master trust measured using fair value shall be presented by general type, such as the following, as of the date of each statement of net assets available for benefits presented:

a. Government securities
b. Short-term securities
c. Corporate bonds
d. Common stocks
e. Mortgages
f. Real estate.
g. Self-directed brokerage accounts (that is, an investment option that allows participants to select investments outside the plan’s core options).

For the presentation of fully benefit-responsive investment contracts, which are measured at contract value, see paragraphs 962-325-35-5A and 962-325-50-3.

Pending Content (Transition Guidance: ASC 962-10-65-4)

50-6 Paragraph superseded by Accounting Standards Update No. 2017-06.

50-7 The total net change in the fair value of investments of the master trust and total investment income of the master trust by type, for example, interest, and dividends, also shall be disclosed in the notes for each period for which a statement of changes in net assets available for benefits is presented.

Pending Content (Transition Guidance: ASC 962-10-65-4)

Interests in Master Trusts

50-7 A plan shall disclose the following in the notes to financial statements for each period for which a statement of changes in net assets available for benefits is presented:

a. Net appreciation or depreciation in the fair value of investments of the master trust. Net appreciation or depreciation includes realized gains and losses on investments that were both purchased and sold during the period as well as unrealized appreciation or depreciation of the investments held at year-end.

b. Investment income (exclusive of (a)).
Appendix A — Fair Value Disclosure Requirements of Other Codification Topics

ASC 962-325 (continued)

Pending Content (Transition Guidance: ASC 962-10-65-4)

50-8A In the notes to financial statements a plan shall include the investments of a master trust measured using fair value presented by general type of investment, such as the following, as of the date of each statement of net assets available for benefits presented:

a. Registered investment companies (for example, mutual funds)

b. Government securities

c. Common-collective trusts

d. Pooled separate accounts

e. Short-term securities

f. Corporate bonds

g. Common stocks

h. Mortgages

i. Real estate

j. Self-directed brokerage accounts (that is, an investment option that allows participants to select investments outside the plan’s core options).

For the presentation of fully benefit-responsive investment contracts, which are measured at contract value, see paragraphs 962-325-35-5A and 962-325-50-3.

Investments Measured Using the Net Asset Value per Share Practical Expedient

50-9 If an investment is measured using the net asset value per share (or its equivalent) practical expedient in paragraph 820-10-35-59 and that investment is in a fund that files U.S. Department of Labor Form 5500 as a direct filing entity, disclosure of that investment’s significant investment strategy, as discussed in paragraph 820-10-50-6A(a), is not required.

A.34 ASC 965, Plan Accounting — Health and Welfare Benefit Plans

ASC 965-20

Statement of Changes in Net Assets Available for Benefits

45-3 The statement of changes in net assets available for benefits shall be presented in enough detail to identify the significant changes during the year, including, as applicable, the following: . . .

e. The net appreciation or depreciation in fair value. Net appreciation or depreciation includes realized gains and losses on investments that were both purchased and sold during the period as well as unrealized appreciation or depreciation of the investments held at year-end.

f. Investment income, excluding the net appreciation or depreciation . . .

45-5 The statement of changes in net assets available for benefits shall be prepared on a basis that reflects income credited to participants in the plan and net appreciation or depreciation in the fair value of only those investment contracts that are not deemed to be fully benefit responsive.
**ASC 965-205**

**50-1** The plan's financial statements shall disclose other information as described in this Subtopic. Certain of the disclosures relate to plans with accumulated assets rather than those with trusts that act more as conduits for benefit payments or insurance premiums. Separate disclosures may be made to the extent that the plan provides both health and other welfare benefits. The disclosures shall include, if applicable, all of the following: . . .

h. Unusual or infrequent events or transactions occurring after the financial statement date, but before the financial statements are issued or are available to be issued (as discussed in Section 855-10-25), that might significantly affect the usefulness of the financial statements in an assessment of the plan's present and future ability to pay benefits. For example, all of the following shall be disclosed:
   1. A plan amendment adopted after the latest financial statement date that significantly increases future benefits attributable to an employee's service rendered before that date
   2. A significant change in the fair value of a significant portion of the plan's assets
   3. The emergence of a catastrophic claim.

If reasonably determinable, the effects of such events or transactions shall be disclosed. If such effects are not reasonably determinable, the reasons why they are not quantifiable shall be disclosed. . . .

**Pending Content (Transition Guidance: ASC 962-10-65-4)**

**401(h) Accounts**

**50-5** A plan is not required to provide investment disclosures (for example, the disclosures required by Topic 815 on derivatives and hedging and Topic 820 on fair value measurement) for 401(h) account assets. A plan shall disclose the name of the defined benefit pension plan that allocated the funds to the health and welfare benefit plan and that provides the related investment disclosures.

**ASC 965-320**

**50-1** Ordinarily, information regarding the net appreciation or depreciation in the fair value less costs to sell, if significant, of investments shall be disclosed in the notes to financial statements.

**ASC 965-325**

**45-1** Information regarding a plan's investments shall be presented in enough detail to identify the types of investments and shall indicate whether reported fair values have been measured by quoted prices in an active market or have been determined otherwise (paragraph 965-325-50-2 specifies additional disclosures related to investments).

**45-2** Investments measured using fair value in the statement of net assets available for benefits or in the notes shall be presented by general type, including the following:

- a. Registered investment companies (also known as mutual funds)
- b. Government securities
- c. Short-term securities
- d. Corporate bonds
- e. Common stocks
- f. Mortgages . . .
- h. Real estate.

For the presentation of fully benefit-responsive investment contracts, which are measured at contract value, see paragraphs 965-325-35-8 and 965-325-50-2.
Disclosure of a health and welfare benefit plan’s accounting policies shall include a description of the valuation techniques and inputs used to measure the fair value less costs to sell, if significant, of investments (as required by Section 820-10-50) and a description of the methods and significant assumptions used to measure the reported value of insurance contracts. However, health and welfare benefit plans are exempt from the requirements in paragraph 820-10-50-2B(a) to disaggregate assets by nature, characteristics, and risks. The disclosures of information by classes of assets required by Section 820-10-50 shall be provided by general type of plan assets consistent with paragraph 965-325-45-2.

Pending Content (Transition Guidance: ASC : 962-10-65-4)

**Interests in Master Trusts**

**50-5** A plan shall disclose the following in the notes to financial statements for each period for which a statement of changes in net assets available for benefits is presented:

- a. Net appreciation or depreciation in the fair value of investments of the master trust. Net appreciation or depreciation includes realized gains and losses on investments that were both purchased and sold during the period as well as unrealized appreciation or depreciation of the investments held at year-end.
- b. Investment income (exclusive of (a)).

**50-7** In the notes to financial statements a plan shall include the investments of a master trust measured using fair value presented by general type of investment, such as the following, as of the date of each statement of net assets available for benefits presented:

- a. Registered investment companies (for example, mutual funds)
- b. Government securities
- c. Common-collective trusts
- d. Pooled separate accounts
- e. Short-term securities
- f. Corporate bonds
- g. Common stocks
- h. Mortgages
- i. Real estate.

For the presentation of fully benefit-responsive investment contracts, which are measured at contract value, see paragraphs 965-325-35-8 and 965-325-50-2.

**Illustrations**

**55-8** See Example 2 (paragraph 962-325-55-17) for financial statements that illustrate certain applications of the provisions of this Subtopic that apply to the annual financial statements of a defined contribution plan.
Appendix B — Comparison of U.S. GAAP and IFRS Standards

ASC 820 is the primary source of guidance on how to measure fair value under U.S. GAAP. IFRS 13 is the primary source of guidance on how to measure fair value under IFRS Standards. IFRS 13 was the result of a joint project between the FASB and the IASB to develop common requirements for measuring fair value and disclosing information about fair value measurements.

The fair value measurement and disclosure requirements under U.S. GAAP are largely converged with, but are not identical to, those under IFRS Standards. For example, the two sets of standards differ with respect to when an entity is required or permitted to measure items at fair value and the extent of the disclosures an entity must provide. Table B-1 below summarizes some of the key differences between IFRS Standards and U.S. GAAP regarding fair value measurement.¹

<table>
<thead>
<tr>
<th>Subject</th>
<th>U.S. GAAP</th>
<th>IFRS Standards</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inception gains and losses (see Section B.1)</td>
<td>If an asset or a liability is measured initially at fair value, any difference between the transaction price and fair value is recognized immediately as a gain or loss in earnings unless otherwise specified.</td>
<td>An entity cannot recognize inception gains or losses for a financial instrument unless the instrument's fair value is demonstrated by a quoted price in an active market for an identical asset or liability or is based on a valuation technique in which an entity uses only observable market data.</td>
</tr>
<tr>
<td>NAV practical expedient (see Section B.2)</td>
<td>An entity with an investment in an investment company may elect to use, as a measure of fair value in specific circumstances, the reported NAV without adjustment.</td>
<td>An NAV practical expedient for investments in investment entities is not provided.</td>
</tr>
<tr>
<td>Disclosures (see Section B.3)</td>
<td>There are differences between the disclosure requirements under U.S. GAAP and those under IFRS Standards. See Section B.3 for more information.</td>
<td></td>
</tr>
</tbody>
</table>

¹ Differences are based on comparison of authoritative literature under U.S. GAAP and IFRS Standards and do not necessarily include interpretations of such literature.
B.1 Inception Gains and Losses

The accounting requirements for inception gains and losses under U.S. GAAP differ from those under IFRS Standards in the following respects:

- Under U.S. GAAP, inception gains and losses may occur if an asset or liability is measured at initial recognition at fair value in the financial statements and the entity acquired or issued the asset or liability at an amount other than fair value (i.e., if the initial transaction price is different from fair value). ASC 820-10-30-6 states that “if another Topic requires or permits a reporting entity to measure an asset or a liability initially at fair value and the transaction price differs from fair value, the reporting entity shall recognize the resulting gain or loss in earnings unless that Topic specifies otherwise.”

- Under IFRS Standards, paragraph B5.1.2A of IFRS 9 prohibits recognition of inception gains or losses for a financial asset or financial liability if fair value is demonstrated by a Level 2 or Level 3 input or is based on a valuation technique in which an entity uses unobservable market data. In such cases, the measurement is adjusted to defer the inception gain or loss. The deferred gain or loss is recognized “only to the extent that it arises from a change in a factor (including time) that market participants would take into account when pricing the asset or liability.”

See Section 9.2.1 for further discussion of the recognition of inception gains and losses under U.S. GAAP.

B.2 NAV Practical Expedient

The accounting requirements for measuring the fair value of investments in investment companies under U.S. GAAP differ from those under IFRS Standards.

- Under U.S. GAAP, ASC 820-10-35-59 contains a practical expedient that permits entities to measure the fair value of an investment that (1) does not have a readily determinable fair value and (2) is in an investment company within the scope of ASC 946 or a real estate fund for which it is industry practice to apply investment-company accounting at NAV.

- The IASB decided against providing any such practical expedient. In the U.S. GAAP–IFRS comparison section in the opening summary in ASU 2011-04, the FASB explains the IASB’s decision as follows:

  [T]he IASB decided that it would be difficult to identify when such a practical expedient could be applied given the different practices for calculating net asset values in jurisdictions around the world. For example, . . . investment companies may report in accordance with national GAAP, which may have recognition and measurement requirements that differ from those in IFRSs (that is, the underlying investments might not be measured at fair value or they might be measured at fair value in accordance with national GAAP, not IFRSs).

See Section 2.2.2 for further discussion of when this practical expedient may be applied under U.S. GAAP.
B.3 Disclosures

As indicated above, the measurement guidance in ASC 820 is largely converged with that in IFRS 13. However, there are differences between the disclosure requirements in ASC 820 and those in IFRS 13, largely because of the guidance in ASU 2018-13. (Very few of these differences existed before ASU 2018-13.) As discussed in Table 11-1 and Section 11.1.2, ASU 2018-13 updated several aspects of the U.S. GAAP fair value disclosure requirements; however, the same updates were not made to IFRS Standards. The Basis for Conclusions of ASU 2018-13 provides the rationale for the divergence between the two sets of standards. Paragraph BC78 of ASU 2018-13 states:

The amendments in this Update relate to disclosures only and remove disclosures that are no longer considered cost beneficial, clarify the specific requirements of disclosures, and add disclosure requirements identified as broadly relevant. The amendments create differences in disclosures based on the FASB's and the IASB's differing assessments on financial statement users' needs and the application of the concepts in the Concepts Statement to the disclosures required by Topic 820.

Therefore, because the disclosure requirements under IFRS 13 and other IFRS Standards differ from those under U.S. GAAP, entities reporting under IFRS Standards should carefully consider these disclosure requirements as part of their annual and interim reporting.

One notable difference between the disclosure requirements under U.S. GAAP and those under IFRS Standards is that IFRS Standards require that entities provide a quantitative sensitivity analysis for recurring fair value measurements of financial instruments classified in Level 3 of the fair value hierarchy. ASU 2018-13 only requires entities that are not nonpublic entities to provide a narrative description of the uncertainty of a Level 3 fair value measurement that results from the use of unobservable inputs if those inputs reasonably could have been different as of the reporting date.
## Appendix C — Glossary of Selected Terms

This appendix contains selected glossary terms from ASC 820 and the ASC master glossary.

<table>
<thead>
<tr>
<th>ASC 820-10 — Glossary and ASC Master Glossary</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Accretion Expense</strong></td>
</tr>
<tr>
<td>An amount recognized as an expense classified as an operating item in the statement of income resulting from the increase in the carrying amount of the liability associated with the asset retirement obligation.</td>
</tr>
</tbody>
</table>

| **Acquiree** |
| The business or businesses that the acquirer obtains control of in a business combination. This term also includes a nonprofit activity or business that a not-for-profit acquirer obtains control of in an acquisition by a not-for-profit entity. |

| **Acquirer** |
| The entity that obtains control of the acquiree. However, in a business combination in which a variable interest entity (VIE) is acquired, the primary beneficiary of that entity always is the acquirer. |

| **Acquisition by a Not-for-Profit Entity** |
| A transaction or other event in which a not-for-profit acquirer obtains control of one or more nonprofit activities or businesses and initially recognizes their assets and liabilities in the acquirer's financial statements. When applicable guidance in Topic 805 is applied by a not-for-profit entity, the term business combination has the same meaning as this term has for a for-profit entity. Likewise, a reference to business combinations in guidance that links to Topic 805 has the same meaning as a reference to acquisitions by not-for-profit entities. |

| **Acquisition Date** |
| The date on which the acquirer obtains control of the acquiree. |

| **Active Market** |
| A market in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. |

| **Actuarial Present Value** |
| The value, as of a specified date, of an amount or series of amounts payable or receivable thereafter, with each amount adjusted to reflect the time value of money (through discounts for interest) and the probability of payment (by means of decrements for events such as death, disability, withdrawal, or retirement) between the specified date and the expected date of payment. |

| **Adequate Compensation** |
| The amount of benefits of servicing that would fairly compensate a substitute servicer should one be required, which includes the profit that would be demanded in the marketplace. It is the amount demanded by the marketplace to perform the specific type of servicing. Adequate compensation is determined by the marketplace; it does not vary according to the specific servicing costs of the servicer. |
## ASC 820-10 — Glossary and ASC Master Glossary (continued)

### Affiliate
A party that, directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with an entity. See Control.

### Affiliated Entity
An entity that directly or indirectly controls, is controlled by, or is under common control with another entity; also, a party with which the entity may deal if one party has the ability to exercise significant influence over the other’s operating and financial policies as discussed in Section 323-10-15.

### Agency Transaction
A type of exchange transaction in which the reporting entity acts as an agent, trustee, or intermediary for another party that may be a donor or donee.

### Agent
**Definition 1**
A party that acts for and on behalf of another party. For example, a third-party intermediary is an agent of the transferor if it acts on behalf of the transferor.

**Definition 2**
An entity that acts for and on behalf of another. Although the term agency has a legal definition, the term is used broadly to encompass not only legal agency, but also the relationships described in Topic 958. A recipient entity acts as an agent for and on behalf of a donor if it receives assets from the donor and agrees to use those assets on behalf of or transfer those assets, the return on investment of those assets, or both to a specified beneficiary. A recipient entity acts as an agent for and on behalf of a beneficiary if it agrees to solicit assets from potential donors specifically for the beneficiary’s use and to distribute those assets to the beneficiary. A recipient entity also acts as an agent if a beneficiary can compel the recipient entity to make distributions to it or on its behalf.

### Allocated Contract
A contract with an insurance entity under which payments to the insurance entity are currently used to purchase immediate or deferred annuities for individual participants. See Annuity Contract.

### Amortized Cost Basis
The amount at which an investment is acquired, adjusted for accretion, amortization, collection of cash, previous other-than-temporary impairments recognized in earnings (less any cumulative-effect adjustments), foreign exchange, and fair value hedge accounting adjustments.

**Note:** The following definition is Pending Content; see Transition Guidance in 326-10-65-1.

The amortized cost basis is the amount at which a financing receivable or investment is originated or acquired, adjusted for applicable accrued interest, accretion, or amortization of premium, discount, and net deferred fees or costs, collection of cash, writeoffs, foreign exchange, and fair value hedge accounting adjustments.

### Annuity Contract
A contract in which an insurance entity unconditionally undertakes a legal obligation to provide specified pension benefits to specific individuals in return for a fixed consideration or premium. An annuity contract is irrevocable and involves the transfer of significant risk from the employer to the insurance entity. Annuity contracts are also called allocated contracts.

### Asset Group
An asset group is the unit of accounting for a long-lived asset or assets to be held and used, which represents the lowest level for which identifiable cash flows are largely independent of the cash flows of other groups of assets and liabilities.
## Appendix C — Glossary of Selected Terms

### ASC 820-10 — Glossary and ASC Master Glossary (continued)

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Asset Retirement Obligation</strong></td>
<td>An obligation associated with the retirement of a tangible long-lived asset.</td>
</tr>
<tr>
<td><strong>Available-for-Sale Securities</strong></td>
<td>Investments not classified as either trading securities or as held-to-maturity securities.</td>
</tr>
<tr>
<td><strong>Bankruptcy Court</strong></td>
<td>The United States Bankruptcy Court is an adjunct of the United States District Courts. Under the jurisdiction of the District Court, the Bankruptcy Court is generally responsible for cases filed under Chapters 7, 11, 12, and 13 of the Bankruptcy Code.</td>
</tr>
<tr>
<td><strong>Benchmark Interest Rate</strong></td>
<td>A widely recognized and quoted rate in an active financial market that is broadly indicative of the overall level of interest rates attributable to high-credit-quality obligors in that market. It is a rate that is widely used in a given financial market as an underlying basis for determining the interest rates of individual financial instruments and commonly referenced in interest-rate-related transactions. In theory, the benchmark interest rate should be a risk-free rate (that is, has no risk of default). In some markets, government borrowing rates may serve as a benchmark. In other markets, the benchmark interest rate may be an interbank offered rate.</td>
</tr>
<tr>
<td><strong>Beneficial Conversion Feature</strong></td>
<td>A nondetachable conversion feature that is in the money at the commitment date.</td>
</tr>
</tbody>
</table>
| **Beneficial Interests** | Rights to receive all or portions of specified cash inflows received by a trust or other entity, including, but not limited to, all of the following:  
  a. Senior and subordinated shares of interest, principal, or other cash inflows to be passed-through or paid-through  
  b. Premiums due to guarantors  
  c. Commercial paper obligations  
  d. Residual interests, whether in the form of debt or equity. |
| **Benefits** | The monetary or in-kind benefits or benefit coverage to which participants may be entitled under a pension plan or a health and welfare plan (which can include active, terminated, and retired employees or their dependents or beneficiaries). Examples of benefits may include, but are not limited to, health care benefits, life insurance, legal, educational, and advisory services, pension benefits, disability benefits, death benefits, and benefits due to termination of employment. |
| **Benefits of Servicing** | Revenues from contractually specified servicing fees, late charges, and other ancillary sources, including float. |
| **Brokered Market** | A market in which brokers attempt to match buyers with sellers but do not stand ready to trade for their own account. In other words, brokers do not use their own capital to hold an inventory of the items for which they make a market. 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. Brokered markets include electronic communication networks, in which buy and sell orders are matched, and commercial and residential real estate markets. |
### ASC 820-10 — Glossary and ASC Master Glossary (continued)

**Business**

Paragraphs 805-10-55-3A through 55-6 and 805-10-55-8 through 55-9 define what is considered a business.

**Business Combination**

A transaction or other event in which an acquirer obtains control of one or more businesses. Transactions sometimes referred to as true mergers or mergers of equals also are business combinations. See also Acquisition by a Not-for-Profit Entity.

**Call Option**

A contract that allows the holder to buy a specified quantity of stock from the writer of the contract at a fixed price for a given period. See Option and Purchased Call Option.

**Capital Lease**

From the perspective of a lessee, a lease that meets any of the four lease classification criteria in paragraph 840-10-25-1.

**Note:** The following definition is Pending Content; see Transition Guidance in 842-10-65-1.

Glossary term superseded by Accounting Standards Update No. 2016-02

**Carrying Amount**

**Definition 1**

For a receivable, the face amount increased or decreased by applicable accrued interest and applicable unamortized premium, discount, finance charges, or issue costs and also an allowance for uncollectible amounts and other valuation accounts.

For a payable, the face amount increased or decreased by applicable accrued interest and applicable unamortized premium, discount, finance charges, or issue costs

**Definition 2**

The amount of an item as displayed in the financial statements.

**Cash**

Consistent with common usage, cash includes not only currency on hand but demand deposits with banks or other financial institutions. Cash also includes other kinds of accounts that have the general characteristics of demand deposits in that the customer may deposit additional funds at any time and also effectively may withdraw funds at any time without prior notice or penalty. All charges and credits to those accounts are cash receipts or payments to both the entity owning the account and the bank holding it. For example, a bank's granting of a loan by crediting the proceeds to a customer's demand deposit account is a cash payment by the bank and a cash receipt of the customer when the entry is made.
**Appendix C — Glossary of Selected Terms**

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**Cash Equivalents**
Cash equivalents are short-term, highly liquid investments that have both of the following characteristics:

- a. Readily convertible to known amounts of cash
- b. So near their maturity that they present insignificant risk of changes in value because of changes in interest rates.

Generally, only investments with original maturities of three months or less qualify under that definition. Original maturity means original maturity to the entity holding the investment. For example, both a three-month U.S. Treasury bill and a three-year U.S. Treasury note purchased three months from maturity qualify as cash equivalents. However, a Treasury note purchased three years ago does not become a cash equivalent when its remaining maturity is three months. Examples of items commonly considered to be cash equivalents are Treasury bills, commercial paper, money market funds, and federal funds sold (for an entity with banking operations).

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**Cash Flow Hedge**
A hedge of the exposure to variability in the cash flows of a recognized asset or liability, or of a forecasted transaction, that is attributable to a particular risk.

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**Cease-Use Date**
The date the entity ceases using the right conveyed by the contract, for example, the right to use a leased property or to receive future goods or services.

---

**Charitable Gift Annuity**
A transfer of assets to a not-for-profit entity (NFP) in connection with a split-interest agreement that is in part a contribution and in part an exchange transaction. The NFP accepts the contribution and is obligated to make periodic stipulated payments to the donor or a third-party beneficiary for a specified period of time, usually either a specified number of years or until the death of the donor or third-party beneficiary.

---

**Charitable Lead Trust**
A trust established in connection with a split-interest agreement, in which a not-for-profit entity (NFP) receives distributions during the agreement's term. Upon termination of the trust, the remainder of the trust assets is paid to the donor or to third-party beneficiaries designated by the donor.

---

**Charitable Remainder Trust**
A trust established in connection with a split-interest agreement, in which the donor or a third-party beneficiary receives specified distributions during the agreement's term. Upon termination of the trust, a not-for-profit entity (NFP) receives the assets remaining in the trust.

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**Collateral**
Personal or real property in which a security interest has been given.

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**Collateral-Dependent Loan**
A loan for which the repayment is expected to be provided solely by the underlying collateral.

**Note:** The following definition is Pending Content; see Transition Guidance in 326-10-65-1

Glossary term superseded by Accounting Standards Update No. 2016-13
<table>
<thead>
<tr>
<th><strong>Collateralized Financing Entity</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>A variable interest entity that holds financial assets, issues beneficial interests in those financial assets, and has no more than nominal equity. The beneficial interests have contractual recourse only to the related assets of the collateralized financing entity and are classified as financial liabilities. A collateralized financing entity may hold nonfinancial assets temporarily as a result of default by the debtor on the underlying debt instruments held as assets by the collateralized financing entity or in an effort to restructure the debt instruments held as assets by the collateralized financing entity. A collateralized financing entity also may hold other financial assets and financial liabilities that are incidental to the operations of the collateralized financing entity and have carrying values that approximate fair value (for example, cash, broker receivables, or broker payables).</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Committed-to-Be-Released Shares</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Committed-to-be-released shares are shares that, although not legally released, will be released by a future scheduled and committed debt service payment and will be allocated to employees for service rendered in the current accounting period. The period of employee service to which shares relate is generally defined in the employee stock ownership plan documents. Shares are legally released from suspense and from serving as collateral for employee stock ownership plan debt as a result of payment of debt service. Those shares are required to be allocated to participant accounts as of the end of the employee stock ownership plan’s fiscal year. Formulas used to determine the number of shares released can be based on either of the following:</td>
</tr>
<tr>
<td>a. The ratio of the current principal amount to the total original principal amount (in which case unearned employee stock ownership plan shares and debt balance will move in tandem)</td>
</tr>
<tr>
<td>b. The ratio of the current principal plus interest amount to the total original principal plus interest to be paid.</td>
</tr>
<tr>
<td>Shares are released more rapidly under the second method than under the first. Tax law permits the first method only if the employee stock ownership plan debt meets certain criteria.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Common Interest Realty Association</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>An association, also known as a community association, responsible for the governance of the common interest community, for which it was established to serve. A common interest realty association is generally funded by its members via periodic assessments by the common interest realty association so that it can perform its duties, which include management services and maintenance, repair, and replacement of the common property, among other duties established in the governing documents and by state statute.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Common Property</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>A common interest realty association's real or personal property to which title or other evidence of ownership is held by either:</td>
</tr>
<tr>
<td>a. Individual members in common</td>
</tr>
<tr>
<td>b. The common interest realty association directly.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Communication Date</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>The date the plan of termination for one-time employee termination benefits meets all of the criteria in paragraph 420-10-25-4 and has been communicated to employees.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Comprehensive Income</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>The change in equity (net assets) of a business entity during a period from transactions and other events and circumstances from nonowner sources. It includes all changes in equity during a period except those resulting from investments by owners and distributions to owners. Comprehensive income comprises both of the following:</td>
</tr>
<tr>
<td>a. All components of net income</td>
</tr>
<tr>
<td>b. All components of other comprehensive income.</td>
</tr>
<tr>
<td><strong>ASC 820-10 — Glossary and ASC Master Glossary (continued)</strong></td>
</tr>
<tr>
<td>---------------------------------------------------------------</td>
</tr>
<tr>
<td><strong>Conditional Asset Retirement Obligation</strong></td>
</tr>
<tr>
<td>A legal obligation to perform an asset retirement activity in</td>
</tr>
<tr>
<td>which the timing and (or) method of settlement are</td>
</tr>
<tr>
<td>conditional on a future event that may or may not be within the</td>
</tr>
<tr>
<td>control of the entity.</td>
</tr>
<tr>
<td><strong>Conditional Contribution</strong></td>
</tr>
<tr>
<td><strong>Note:</strong> The following definition is Pending Content; see</td>
</tr>
<tr>
<td>A contribution that contains a donor-imposed condition.</td>
</tr>
<tr>
<td><strong>Conduit Debt Securities</strong></td>
</tr>
<tr>
<td>Certain limited-obligation revenue bonds, certificates of</td>
</tr>
<tr>
<td>participation, or similar debt instruments issued by a</td>
</tr>
<tr>
<td>state or local governmental entity for the express purpose of</td>
</tr>
<tr>
<td>providing financing for a specific third party (the conduit</td>
</tr>
<tr>
<td>bond obligor) that is not a part of the state or local</td>
</tr>
<tr>
<td>government's financial reporting entity. Although conduit</td>
</tr>
<tr>
<td>debt securities bear the name of the governmental entity that</td>
</tr>
<tr>
<td>issues them, the governmental entity often has no obligation</td>
</tr>
<tr>
<td>for such debt beyond the resources provided by a lease or loan</td>
</tr>
<tr>
<td>agreement with the third party on whose behalf the securities</td>
</tr>
<tr>
<td>are issued. Further, the conduit bond obligor is responsible for</td>
</tr>
<tr>
<td>any future financial reporting requirements.</td>
</tr>
<tr>
<td><strong>Contingency</strong></td>
</tr>
<tr>
<td>An existing condition, situation, or set of circumstances</td>
</tr>
<tr>
<td>involving uncertainty as to possible gain (gain contingency) or</td>
</tr>
<tr>
<td>loss (loss contingency) to an entity that will ultimately be</td>
</tr>
<tr>
<td>resolved when one or more future events occur or fail to occur.</td>
</tr>
<tr>
<td><strong>Contingent Consideration</strong></td>
</tr>
<tr>
<td>Usually an obligation of the acquirer to transfer additional</td>
</tr>
<tr>
<td>assets or equity interests to the former owners of an acquiree</td>
</tr>
<tr>
<td>as part of the exchange for control of the acquiree if specified</td>
</tr>
<tr>
<td>future events occur or conditions are met. However, contingent</td>
</tr>
<tr>
<td>consideration also may give the acquirer the right to the return</td>
</tr>
<tr>
<td>of previously transferred consideration if specified conditions</td>
</tr>
<tr>
<td>are met.</td>
</tr>
<tr>
<td><strong>Continuing Involvement</strong></td>
</tr>
<tr>
<td>Any involvement with the transferred financial assets that</td>
</tr>
<tr>
<td>permits the transferor to receive cash flows or other benefits</td>
</tr>
<tr>
<td>that arise from the transferred financial assets or that</td>
</tr>
<tr>
<td>obligates the transferor to provide additional cash flows or</td>
</tr>
<tr>
<td>other assets to any party related to the transfer. For related</td>
</tr>
<tr>
<td>implementation guidance, see paragraph 860-10-55-79A.</td>
</tr>
<tr>
<td><strong>Contract</strong></td>
</tr>
<tr>
<td>An agreement between two or more parties that creates enforceable</td>
</tr>
<tr>
<td>rights and obligations.</td>
</tr>
<tr>
<td><strong>Contract Value</strong></td>
</tr>
<tr>
<td>The value of an unallocated contract that is determined by the</td>
</tr>
<tr>
<td>insurance entity in accordance with the terms of the contract.</td>
</tr>
<tr>
<td><strong>Contractually Required Payments Receivable</strong></td>
</tr>
<tr>
<td>The total undiscounted amount of all uncollected contractual</td>
</tr>
<tr>
<td>principal and contractual interest payments both past due and</td>
</tr>
<tr>
<td>scheduled for the future, adjusted for the timing of prepayments,</td>
</tr>
<tr>
<td>if considered, less any reduction by the investor. For an</td>
</tr>
<tr>
<td>acquired asset-backed security with required contractual</td>
</tr>
<tr>
<td>payments of principal and interest, the contractually required</td>
</tr>
<tr>
<td>payments receivable is represented by the contractual terms of</td>
</tr>
<tr>
<td>the security. However, when contractual payments of principal</td>
</tr>
<tr>
<td>and interest are not specified by the security, it is necessary</td>
</tr>
<tr>
<td>to consider the contractual terms of the underlying loans or</td>
</tr>
<tr>
<td>assets.</td>
</tr>
</tbody>
</table>
ASC 820-10 — Glossary and ASC Master Glossary (continued)

**Contractually Specified Servicing Fees**

All amounts that, per contract, are due to the servicer in exchange for servicing the financial asset and would no longer be received by a servicer if the beneficial owners of the serviced assets (or their trustees or agents) were to exercise their actual or potential authority under the contract to shift the servicing to another servicer. Depending on the servicing contract, those fees may include some or all of the difference between the interest rate collectible on the financial asset being serviced and the rate to be paid to the beneficial owners of those financial assets.

**Contribution**

**Note:** The following definition is Pending Content; see Transition Guidance in 958-10-65-2.

An unconditional transfer of cash or other assets, as well as unconditional promises to give, to an entity or a reduction, settlement, or cancellation of its liabilities in a voluntary nonreciprocal transfer by another entity acting other than as an owner. Those characteristics distinguish contributions from:

- a. Exchange transactions, which are reciprocal transfers in which each party receives and sacrifices approximately commensurate value
- b. Investments by owners and distributions to owners, which are nonreciprocal transfers between an entity and its owners
- c. Other nonreciprocal transfers, such as impositions of taxes or legal judgments, fines, and thefts, which are not voluntary transfers.

In a contribution transaction, the resource provider often receives value indirectly by providing a societal benefit although that benefit is not considered to be of commensurate value. In an exchange transaction, the potential public benefits are secondary to the potential direct benefits to the resource provider. The term **contribution revenue** is used to apply to transactions that are part of the entity's ongoing major or central activities (revenues), or are peripheral or incidental to the entity (gains). See also Inherent Contribution and Conditional Contribution.

**Contributory Plan**

A plan under which retirees or active employees contribute part of the cost. In some contributory plans, retirees or active employees wishing to be covered must contribute; in other contributory plans, participants' contributions result in increased benefits.

**Control**

**Definition 1**

The possession, direct or indirect, of the power to direct or cause the direction of the management and policies of an entity through ownership, by contract, or otherwise.

**Definition 2**

The direct or indirect ability to determine the direction of management and policies through ownership, contract, or otherwise.

**Definition 3**

The same as the meaning of controlling financial interest in paragraph 810-10-15-8.
Corporate Joint Venture
A corporation owned and operated by a small group of entities (the joint venturers) as a separate and specific business or project for the mutual benefit of the members of the group. A government may also be a member of the group. The purpose of a corporate joint venture frequently is to share risks and rewards in developing a new market, product or technology; to combine complementary technological knowledge; or to pool resources in developing production or other facilities. A corporate joint venture also usually provides an arrangement under which each joint venturer may participate, directly or indirectly, in the overall management of the joint venture. Joint venturers thus have an interest or relationship other than as passive investors. An entity that is a subsidiary of one of the joint venturers is not a corporate joint venture. The ownership of a corporate joint venture seldom changes, and its stock is usually not traded publicly. A noncontrolling interest held by public ownership, however, does not preclude a corporation from being a corporate joint venture.

Cost Approach
A valuation approach that reflects the amount that would be required currently to replace the service capacity of an asset (often referred to as current replacement cost).

Credit Derivative
A derivative instrument that has both of the following characteristics:

a. One or more of its underlyings are related to any of the following:
   1. The credit risk of a specified entity (or a group of entities)
   2. An index based on the credit risk of a group of entities.

b. It exposes the seller to potential loss from credit-risk-related events specified in the contract.

Examples of credit derivatives include, but are not limited to, credit default swaps, credit spread options, and credit index products.

Credit Risk
For purposes of a hedged item in a fair value hedge, credit risk is the risk of changes in the hedged item's fair value attributable to both of the following:

a. Changes in the obligor's creditworthiness
b. Changes in the spread over the benchmark interest rate with respect to the hedged item's credit sector at inception of the hedge.

For purposes of a hedged transaction in a cash flow hedge, credit risk is the risk of changes in the hedged transaction's cash flows attributable to all of the following:

a. Default
b. Changes in the obligor's creditworthiness
c. Changes in the spread over the benchmark interest rate with respect to the related financial asset's or liability's credit sector at inception of the hedge.

Note: The following definition is Pending Content; see Transition Guidance in 815-20-65-3.

For purposes of a hedged item in a fair value hedge, credit risk is the risk of changes in the hedged item's fair value attributable to both of the following:

a. Changes in the obligor's creditworthiness
b. Changes in the spread over the benchmark interest rate with respect to the hedged item's credit sector at inception of the hedge.
### Currency Risk
The risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

### Customer
A party that has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for consideration.

### Dealer Market
A market in which dealers stand ready to trade (either buy or sell for their own account), thereby providing liquidity by using their capital to hold an inventory of the items for which they make a market. Typically, bid and ask prices (representing the price at which the dealer is willing to buy and the price at which the dealer is willing to sell, respectively) are more readily available than closing prices. Over-the-counter markets (for which prices are publicly reported by the National Association of Securities Dealers Automated Quotations systems or by OTC Markets Group Inc.) are dealer markets. For example, the market for U.S. Treasury securities is a dealer market. Dealer markets also exist for some other assets and liabilities, including other financial instruments, commodities, and physical assets (for example, used equipment).

### Debt Security
Any security representing a creditor relationship with an entity. The term debt security also includes all of the following:

- Preferred stock that by its terms either must be redeemed by the issuing entity or is redeemable at the option of the investor
- A collateralized mortgage obligation (or other instrument) that is issued in equity form but is required to be accounted for as a nonequity instrument regardless of how that instrument is classified (that is, whether equity or debt) in the issuer's statement of financial position
- U.S. Treasury securities
- U.S. government agency securities
- Municipal securities
- Corporate bonds
- Convertible debt
- Commercial paper
- All securitized debt instruments, such as collateralized mortgage obligations and real estate mortgage investment conduits
- Interest-only and principal-only strips.
The term debt security excludes all of the following:

- Option contracts
- Financial futures contracts
- Forward contracts
- Lease contracts
- Receivables that do not meet the definition of security and, so, are not debt securities, for example:
  1. Trade accounts receivable arising from sales on credit by industrial or commercial entities
  2. Loans receivable arising from consumer, commercial, and real estate lending activities of financial institutions.

**Debt-Equity Swap**

A debt-equity swap is an exchange transaction of a monetary asset for a nonmonetary asset.

**Defensive Intangible Asset**

An acquired intangible asset in a situation in which an entity does not intend to actively use the asset but intends to hold (lock up) the asset to prevent others from obtaining access to the asset.

**Defined Benefit Plan**

A defined benefit plan provides participants with a determinable benefit based on a formula provided for in the plan.

- Defined benefit health and welfare plans — Defined benefit health and welfare plans specify a determinable benefit, which may be in the form of a reimbursement to the covered plan participant or a direct payment to providers or third-party insurers for the cost of specified services. Such plans may also include benefits that are payable as a lump sum, such as death benefits. The level of benefits may be defined or limited based on factors such as age, years of service, and salary. Contributions may be determined by the plan's actuary or be based on premiums, actual claims paid, hours worked, or other factors determined by the plan sponsor. Even when a plan is funded pursuant to agreements that specify a fixed rate of employer contributions (for example, a collectively bargained multiemployer plan), such a plan may nevertheless be a defined benefit health and welfare plan if its substance is to provide a defined benefit.

- Defined benefit pension plan — A pension plan that defines an amount of pension benefit to be provided, usually as a function of one or more factors such as age, years of service, or compensation. Any pension plan that is not a defined contribution pension plan is, for purposes of Subtopic 715-30, a defined benefit pension plan.

- Defined benefit postretirement plan — A plan that defines postretirement benefits in terms of monetary amounts (for example, $100,000 of life insurance) or benefit coverage to be provided (for example, up to $200 per day for hospitalization, or 80 percent of the cost of specified surgical procedures). Any postretirement benefit plan that is not a defined contribution postretirement plan is, for purposes of Subtopic 715-60, a defined benefit postretirement plan. (Specified monetary amounts and benefit coverage are collectively referred to as benefits.)
ASC 820-10 — Glossary and ASC Master Glossary (continued)

**Defined Contribution Plan**
A plan that provides an individual account for each participant and provides benefits that are based on all of the following: amounts contributed to the participant's account by the employer or employee; investment experience; and any forfeitures allocated to the account, less any administrative expenses charged to the plan.

a. Defined contribution health and welfare plans — Defined contribution health and welfare plans maintain an individual account for each plan participant. They have terms that specify the means of determining the contributions to participants' accounts, rather than the amount of benefits the participants are to receive. The benefits a plan participant will receive are limited to the amount contributed to the participant's account, investment experience, expenses, and any forfeitures allocated to the participant's account. These plans also include flexible spending arrangements.

b. Defined contribution postretirement plan — A plan that provides postretirement benefits in return for services rendered, provides an individual account for each plan participant, and specifies how contributions to the individual's account are to be determined rather than specifies the amount of benefits the individual is to receive. Under a defined contribution postretirement plan, the benefits a plan participant will receive depend solely on the amount contributed to the plan participant's account, the returns earned on investments of those contributions, and the forfeitures of other plan participants' benefits that may be allocated to that plan participant's account.

**Derecognize**
Remove previously recognized assets or liabilities from the statement of financial position.

**Derivative Financial Instrument**
A derivative instrument that is a financial instrument.

**Derivative Instrument**
Paragraphs 815-10-15-83 through 15-139 define the term *derivative instrument*.

**Direct Financing Lease**
**Note:** The following definition is Pending Content; see Transition Guidance in 842-10-65-1.

From the perspective of a lessor, a lease that meets none of the criteria in paragraph 842-10-25-2 but meets the criteria in paragraph 842-10-25-3(b).

**Direct Financing Leases**
From the perspective of a lessor, a lease that meets all of the conditions in paragraph 840-10-25-43(b).

**Note:** The following definition is Pending Content; see Transition Guidance in 842-10-65-1.

Glossary term superseded by Accounting Standards Update No. 2016-02

**Discount Rate**
A rate or rates used to reflect the time value of money. Discount rates are used in determining the present value as of the measurement date of future cash flows currently expected to be required to satisfy the pension obligation or other postretirement benefit obligation. See Actuarial Present Value.

**Discount Rate Adjustment Technique**
A present value technique that uses a risk-adjusted discount rate and contractual, promised, or most likely cash flows.
### ASC 820-10 — Glossary and ASC Master Glossary (continued)

#### Disposal Group
A disposal group for a long-lived asset or assets to be disposed of by sale or otherwise represents assets to be disposed of together as a group in a single transaction and liabilities directly associated with those assets that will be transferred in the transaction. A disposal group may include a discontinued operation along with other assets and liabilities that are not part of the discontinued operation.

#### Donor-Imposed Condition
A donor stipulation that specifies a future and uncertain event whose occurrence or failure to occur gives the promisor a right of return of the assets it has transferred or releases the promisor from its obligation to transfer its assets.

**Note:** The following definition is Pending Content; see Transition Guidance in 958-10-65-2.

A donor stipulation (donors include other types of contributors, including makers of certain grants) that represents a barrier that must be overcome before the recipient is entitled to the assets transferred or promised. Failure to overcome the barrier gives the contributor a right of return of the assets it has transferred or gives the promisor a right of release from its obligation to transfer its assets.

#### Donor-Imposed Restriction
A donor stipulation (donors include other types of contributors, including makers of certain grants) that specifies a use for a contributed asset that is more specific than broad limits resulting from the following:

- a. The nature of the not-for-profit entity (NFP)
- b. The environment in which it operates
- c. The purposes specified in its articles of incorporation or bylaws or comparable documents for an unincorporated association.

Some donors impose restrictions that are temporary in nature, for example, stipulating that resources be used after a specified date, for particular programs or services, or to acquire buildings or equipment. Other donors impose restrictions that are perpetual in nature, for example, stipulating that resources be maintained in perpetuity. Laws may extend those limits to investment returns from those resources and to other enhancements (diminishments) of those resources. Thus, those laws extend donor-imposed restrictions.

#### Embedded Credit Derivative
An embedded derivative that is also a credit derivative.

#### Embedded Derivative
Implicit or explicit terms that affect some or all of the cash flows or the value of other exchanges required by a contract in a manner similar to a derivative instrument.

#### Employee Stock Ownership Plan
An employee stock ownership plan is an employee benefit plan that is described by the Employee Retirement Income Security Act of 1974 and the Internal Revenue Code of 1986 as a stock bonus plan, or combination stock bonus and money purchase pension plan, designed to invest primarily in employer stock. Also called an employee share ownership plan.

#### Entry Price
The price paid to acquire an asset or received to assume a liability in an exchange transaction.

#### Equity Interests
Used broadly to mean ownership interests of investor-owned entities; owner, member, or participant interests of mutual entities; and owner or member interests in the net assets of not-for-profit entities.
### ASC 820-10 — Glossary and ASC Master Glossary (continued)

#### Equity Security

**Definition 1**

Any security representing an ownership interest in an entity (for example, common, preferred, or other capital stock) or the right to acquire (for example, warrants, rights, forward purchase contracts, and call options) or dispose of (for example, put options and forward sale contracts) an ownership interest in an entity at fixed or determinable prices. The term equity security does not include any of the following:

- a. Written equity options (because they represent obligations of the writer, not investments)
- b. Cash-settled options on equity securities or options on equity-based indexes (because those instruments do not represent ownership interests in an entity)
- c. Convertible debt or preferred stock that by its terms either must be redeemed by the issuing entity or is redeemable at the option of the investor

**Definition 2**

Any security representing an ownership interest in an entity (for example, common, preferred, or other capital stock) or the right to acquire (for example, warrants, rights, forward purchase contracts, and call options) or dispose of (for example, put options and forward sale contracts) an ownership interest in an entity at fixed or determinable prices. However, the term does not include convertible debt or preferred stock that by its terms either must be redeemed by the issuing entity or is redeemable at the option of the investor.

#### Exchange

An exchange (or exchange transaction) is a reciprocal transfer between two entities that results in one of the entities acquiring assets or services or satisfying liabilities by surrendering other assets or services or incurring other obligations.

#### Exchange Market

A market in which closing prices are both readily available and generally representative of fair value. An example of such a market is the New York Stock Exchange.

#### Exit Price

The price that would be received to sell an asset or paid to transfer a liability.

#### Expected Cash Flow

The probability-weighted average (that is, mean of the distribution) of possible future cash flows.

#### Fail-to-Receive

A fail-to-receive is a securities purchase from another broker-dealer not received from the selling broker-dealer by the close of business on the settlement date.

#### Fair Value

The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

#### Fair Value Hedge

A hedge of the exposure to changes in the fair value of a recognized asset or liability, or of an unrecognized firm commitment, that are attributable to a particular risk.
### Appendix C — Glossary of Selected Terms

**ASC 820-10 — Glossary and ASC Master Glossary (continued)**

**Fair Value of Leased Property**
The price for which the property could be sold in an arm's-length transaction between unrelated parties.

**Note:** The following definition is Pending Content; see Transition Guidance in 842-10-65-1.

Glossary term superseded by Accounting Standards Update No. 2016-02

**Federal Home Loan Mortgage Corporation**
Often referred to as Freddie Mac, FHLMC is a private corporation authorized by Congress to assist in the development and maintenance of a secondary market in conventional residential mortgages. FHLMC purchases mortgage loans and sells mortgages principally through mortgage participation certificates representing an undivided interest in a group of conventional mortgages. FHLMC guarantees the timely payment of interest and the collection of principal on the participation certificates.

**Federal National Mortgage Association**
Often referred to as Fannie Mae, FNMA is an investor-owned corporation established by Congress to support the secondary mortgage loan market by purchasing mortgage loans when other investor funds are limited and selling mortgage loans when other investor funds are available.

**Film Group**

**Note:** The following definition is Pending Content; see Transition Guidance in 926-20-65-2.

The unit of account used for impairment testing for a film or a license agreement for program material when the film or license agreement is expected to be predominantly monetized with other films and/or license agreements instead of being predominantly monetized on its own. A film group represents the lowest level for which identifiable cash flows are largely independent of the cash flows of other films and/or license agreements.

**Films**

Feature films, television specials, television series, or similar products (including animated films and television programming) that are sold, licensed, or exhibited, whether produced on film, video tape, digital, or other video recording format.

**Finance Lease**

**Note:** The following definition is Pending Content; see Transition Guidance in 842-10-65-1.

From the perspective of a lessee, a lease that meets one or more of the criteria in paragraph 842-10-25-2.

**Financial Asset**
Cash, evidence of an ownership interest in an entity, or a contract that conveys to one entity a right to do either of the following:

- Receive cash or another financial instrument from a second entity
- Exchange other financial instruments on potentially favorable terms with the second entity.
ASC 820-10 — Glossary and ASC Master Glossary (continued)

Financial Instrument
Cash, evidence of an ownership interest in an entity, or a contract that both:

a. Imposes on one entity a contractual obligation either:
   1. To deliver cash or another financial instrument to a second entity
   2. To exchange other financial instruments on potentially unfavorable terms with the second entity.

b. Conveys to that second entity a contractual right either:
   1. To receive cash or another financial instrument from the first entity
   2. To exchange other financial instruments on potentially favorable terms with the first entity.

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.

Contractual rights and contractual obligations encompass both those that are conditioned on the occurrence of a specified event and those that are not. All contractual rights (contractual obligations) that are financial instruments meet the definition of asset (liability) set forth in FASB Concepts Statement No. 6, Elements of Financial Statements, although some may not be recognized as assets (liabilities) in financial statements — that is, they 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 (or the obligation is owed to or by) a group of entities rather than a single entity.

Financial Liability
A contract that imposes on one entity an obligation to do either of the following:

a. Deliver cash or another financial instrument to a second entity

b. Exchange other financial instruments on potentially unfavorable terms with the second entity.

Financial Statements Are Available to Be Issued
Financial statements are considered available to be issued when they are complete in a form and format that complies with GAAP and all approvals necessary for issuance have been obtained, for example, from management, the board of directors, and/or significant shareholders. The process involved in creating and distributing the financial statements will vary depending on an entity’s management and corporate governance structure as well as statutory and regulatory requirements.
Firm Commitment

Definition 1
An agreement with a third party that is binding on both parties. The agreement specifies all significant terms, including items to be exchanged, consideration, and timing of the transaction. The agreement includes a disincentive for nonperformance that is sufficiently large to ensure the expected performance. In the context of episodic television series, a firm commitment for future production includes only episodes to be delivered within one year from the date of the estimate of ultimate revenue.

Definition 2
An agreement with an unrelated party, binding on both parties and usually legally enforceable, with the following characteristics:

- The agreement specifies all significant terms, including the quantity to be exchanged, the fixed price, and the timing of the transaction. The fixed price may be expressed as a specified amount of an entity's functional currency or of a foreign currency. It may also be expressed as a specified interest rate or specified effective yield. The binding provisions of an agreement are regarded to include those legal rights and obligations codified in the laws to which such an agreement is subject. A price that varies with the market price of the item that is the subject of the firm commitment cannot qualify as a fixed price. For example, a price that is specified in terms of ounces of gold would not be a fixed price if the market price of the item to be purchased or sold under the firm commitment varied with the price of gold.

- The agreement includes a disincentive for nonperformance that is sufficiently large to make performance probable. In the legal jurisdiction that governs the agreement, the existence of statutory rights to pursue remedies for default equivalent to the damages suffered by the nondefaulting party, in and of itself, represents a sufficiently large disincentive for nonperformance to make performance probable for purposes of applying the definition of a firm commitment.

Forward Commitment Dollar Roll
See Government National Mortgage Association Rolls.

Forward Exchange Contract
A forward exchange contract is an agreement between two parties to exchange different currencies at a specified exchange rate at an agreed-upon future date.

Freestanding Financial Instrument
A financial instrument that meets either of the following conditions:

- It is entered into separately and apart from any of the entity’s other financial instruments or equity transactions.

- It is entered into in conjunction with some other transaction and is legally detachable and separately exercisable.
ASC 820-10 — Glossary and ASC Master Glossary (continued)

Fully Benefit-Responsive Investment Contract

An investment contract is considered fully benefit-responsive if all of the following criteria are met for that contract, analyzed on an individual basis:

a. The investment contract is effected directly between the plan and the issuer and prohibits the plan from assigning or selling the contract or its proceeds to another party without the consent of the issuer.

b. Either of the following conditions exists:
   1. The repayment of principal and interest credited to participants in the plan is a financial obligation of the issuer of the investment contract.
   2. Prospective interest crediting rate adjustments are provided to participants in the plan on a designated pool of investments held by the plan or the contract issuer, whereby a financially responsible third party, through a contract generally referred to as a wrapper, must provide assurance that the adjustments to the interest crediting rate will not result in a future interest crediting rate that is less than zero.

If an event has occurred such that realization of full contract value for a particular investment contract is no longer probable (for example, a significant decline in creditworthiness of the contract issuer or wrapper provider), the investment contract shall no longer be considered fully benefit-responsive.

c. The terms of the investment contract require all permitted participant-initiated transactions with the plan to occur at contract value with no conditions, limits, or restrictions. Permitted participant-initiated transactions are those transactions allowed by the plan, such as any of the following:
   1. Withdrawals for benefits
   2. Loans
   3. Transfers to other funds within the plan.

d. An event that limits the ability of the plan to transact at contract value with the issuer and that also limits the ability of the plan to transact at contract value with the participants in the plan, such as any of the following, must be probable of not occurring:
   1. Premature termination of the contracts by the plan
   2. Plant closings
   3. Layoffs
   4. Plan termination
   5. Bankruptcy
   6. Mergers
   7. Early retirement incentives.

e. The plan itself must allow participants reasonable access to their funds.

If access to funds is substantially restricted by plan provisions, investment contracts held by those plans may not be considered to be fully benefit-responsive. For example, if plan participants are allowed access at contract value to all or a portion of their account balances only upon termination of their participation in the plan, it would not be considered reasonable access and, therefore, investment contracts held by that plan would generally not be deemed to be fully benefit-responsive. However, in plans with a single investment fund that allow reasonable access to assets by inactive participants, restrictions on access to assets by active participants consistent with the objective of the plan (for example, retirement or health and welfare benefits) will not affect the benefit responsiveness of the investment contracts held by those single-fund plans. Also, if a plan limits participants' access to their account balances to certain specified times during the plan year (for example, semiannually or quarterly) to control the administrative costs of the plan, that limitation generally would not affect the benefit responsiveness of the investment contracts held by that plan. In addition, administrative provisions that place short-term restrictions (for example, three or six months) on transfers to competing fixed-rate investment options to limit arbitrage among those investment options (equity wash provisions) would not affect a contract's benefit responsiveness.
**Gain Contingency**
An existing condition, situation, or set of circumstances involving uncertainty as to possible gain to an entity that will ultimately be resolved when one or more future events occur or fail to occur.

**General Account**

**Definition 1**
An undivided fund maintained by an insurance entity that commingles plan assets with other assets of the insurance entity for investment purposes. That is, funds held by an insurance entity that are not maintained in a separate account are in its general account.

**Definition 2**
All operations of an insurance entity that are not reported in the separate account(s).

**Goodwill**
An asset representing the future economic benefits arising from other assets acquired in a business combination or an acquisition by a not-for-profit entity that are not individually identified and separately recognized. For ease of reference, this term also includes the immediate charge recognized by not-for-profit entities in accordance with paragraph 958-805-25-29.

**Government National Mortgage Association**
Often referred to as Ginnie Mae, GNMA is a U.S. governmental agency that guarantees certain types of mortgage-backed securities and provides funds for and administers certain types of low-income housing assistance programs.

**Government National Mortgage Association Rolls**
The term Government National Mortgage Association (GNMA) rolls has been used broadly to refer to a variety of transactions involving mortgage-backed securities, frequently those issued by the GNMA. There are four basic types of transactions:

a. Type 1. Reverse repurchase agreements for which the exact same security is received at the end of the repurchase period (vanilla repo)

b. Type 2. Fixed coupon dollar reverse repurchase agreements (dollar repo)

c. Type 3. Fixed coupon dollar reverse repurchase agreements that are rolled at their maturities, that is, renewed in lieu of taking delivery of an underlying security (GNMA roll)

d. Type 4. Forward commitment dollar rolls (also referred to as to-be-announced GNMA forward contracts or to-be-announced GNMA rolls), for which the underlying security does not yet exist.

**Group Participating Pension Contracts**
Contracts between insurance entities and pension plans that have account balance crediting provisions that give the contract holder the total return based on a referenced pool of assets over the life of the contract either through crediting rates or termination adjustments.
Health and Welfare Benefit Plans
Health and welfare benefit plans include plans that provide the following:

- Any of the following benefits:
  1. Medical, dental, visual, psychiatric, or long-term health care
  2. Life insurance (offered separately from a pension plan)
  3. Certain severance benefits
  4. Accidental death or dismemberment benefits.
- Benefits for unemployment, disability, vacations, or holidays
- Other benefits such as apprenticeships, tuition assistance, day care, dependent care, housing subsidies, or legal services.

Highest and Best Use
The use of a nonfinancial asset by market participants that would maximize the value of the asset or the group of assets and liabilities (for example, a business) within which the asset would be used.

Hybrid Instrument
A contract that embodies both an embedded derivative and a host contract.

Identifiable
An asset is identifiable if it meets either of the following criteria:

- It is separable, that is, capable of being separated or divided from the entity and sold, transferred, licensed, rented, or exchanged, either individually or together with a related contract, identifiable asset, or liability, regardless of whether the entity intends to do so.
- It arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

Impairment
Impairment is the condition that exists when the carrying amount of a long-lived asset (asset group) exceeds its fair value.

Income Approach
Valuation approaches that convert future amounts (for example, cash flows or income and expenses) to a single current (that is, discounted) amount. The fair value measurement is determined on the basis of the value indicated by current market expectations about those future amounts.

Inherent Contribution
A contribution that results if an entity voluntarily transfers assets (or net assets) or performs services for another entity in exchange for either no assets or for assets of substantially lower value and unstated rights or privileges of a commensurate value are not involved.

Inputs
The assumptions that market participants would use when pricing the asset or liability, including assumptions about risk, such as the following:

- The risk inherent in a particular valuation technique used to measure fair value (such as a pricing model)
- The risk inherent in the inputs to the valuation technique.

Inputs may be observable or unobservable.
Appendix C — Glossary of Selected Terms

**ASC 820-10 — Glossary and ASC Master Glossary (continued)**

**Insurance Contract**
A contract in which an insurance entity unconditionally undertakes a legal obligation to provide specified benefits to specific individuals in return for a fixed consideration or premium. An insurance contract is irrevocable and involves the transfer of significant risk from the employer (or the plan) to the insurance entity.

**Intangible Assets**
Assets (not including financial assets) that lack physical substance. (The term intangible assets is used to refer to intangible assets other than goodwill.)

**Interest Rate Risk**
The risk of changes in a hedged item's fair value or cash flows attributable to changes in the designated benchmark interest rate.

**Note:** The following definition is Pending Content; see Transition Guidance in 815-20-65-3.

For recognized variable-rate financial instruments and forecasted issuances or purchases of variable-rate financial instruments, interest rate risk is the risk of changes in the hedged item's cash flows attributable to changes in the contractually specified interest rate in the agreement.

For recognized fixed-rate financial instruments, interest rate risk is the risk of changes in the hedged item's fair value attributable to changes in the designated benchmark interest rate. For forecasted issuances or purchases of fixed-rate financial instruments, interest rate risk is the risk of changes in the hedged item's cash flows attributable to changes in the designated benchmark interest rate.

**Intermediary**
Although in general usage the term intermediary encompasses a broad range of situations in which an entity acts between two or more other parties, in this usage, it refers to situations in which a recipient entity acts as a facilitator for the transfer of assets between a potential donor and a potential beneficiary (donee) but is neither an agent or trustee nor a donee and donor.

**Investee**
An entity that issued an equity instrument that is held by an investor.

**Issuer**
The entity that issued a financial instrument or may be required under the terms of a financial instrument to issue its equity shares.

**Issuer's Equity Shares**
The equity shares of any entity whose financial statements are included in the consolidated financial statements.

**Lead Interest**
The right to the benefits (cash flows or use) of assets during the term of a split-interest agreement, which generally starts upon the signing of the agreement and terminates at either of the following times:

a. After a specified number of years (period-certain)

b. Upon the occurrence of a certain event, commonly either the death of the donor or the death of the lead interest beneficiary (life-contingent).
Lease
An agreement conveying the right to use property, plant, or equipment (land and/or depreciable assets) usually for a stated period of time.

Note: The following definition is Pending Content; see Transition Guidance in 842-10-65-1.
A contract, or part of a contract, that conveys the right to control the use of identified property, plant, or equipment (an identified asset) for a period of time in exchange for consideration.

Legal Entity
Any legal structure used to conduct activities or to hold assets. Some examples of such structures are corporations, partnerships, limited liability companies, grantor trusts, and other trusts.

Legal Obligation
An obligation that a party is required to settle as a result of an existing or enacted law, statute, ordinance, or written or oral contract or by legal construction of a contract under the doctrine of promissory estoppel.

Lessee
Note: The following definition is Pending Content; see Transition Guidance in 842-10-65-1.
An entity that enters into a contract to obtain the right to use an underlying asset for a period of time in exchange for consideration.

Lessor
Note: The following definition is Pending Content; see Transition Guidance in 842-10-65-1.
An entity that enters into a contract to provide the right to use an underlying asset for a period of time in exchange for consideration.

Level 1 Inputs
Quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date.

Level 2 Inputs
Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 Inputs
Unobservable inputs for the asset or liability.

Liability Issued With an Inseparable Third-Party Credit Enhancement
A liability that is issued with a credit enhancement obtained from a third party, such as debt that is issued with a financial guarantee from a third party that guarantees the issuer’s payment obligation.

License Agreement
A typical license agreement for program material (for example, features, specials, series, or cartoons) covers several programs (a package) and grants a television station, group of stations, network, pay television, or cable television system (licensee) the right to broadcast either a specified number or an unlimited number of showings over a maximum period of time (license period) for a specified fee.
**Life Settlement Contract**

A life settlement contract is a contract between the owner of a life insurance policy (the policy owner) and a third-party investor (investor), and has all of the following characteristics:

- The investor does not have an insurable interest (an interest in the survival of the insured, which is required to support the issuance of an insurance policy).
- The investor provides consideration to the policy owner of an amount in excess of the current cash surrender value of the life insurance policy.
- The contract pays the face value of the life insurance policy to an investor when the insured dies.

**Liquidity**

An asset's or liability's nearness to cash. Donor-imposed restrictions may influence the liquidity or cash flow patterns of certain assets. For example, a donor stipulation that donated cash be used to acquire land and buildings limits an entity's ability to take effective actions to respond to unexpected opportunities or needs, such as emergency disaster relief. On the other hand, some donor-imposed restrictions have little or no influence on cash flow patterns or an entity's financial flexibility. For example, a gift of cash with a donor stipulation that it be used for emergency-relief efforts has a negligible impact on an entity if emergency relief is one of its major ongoing programs.

**Loan**

**Definition 1**

A contractual right to receive money on demand or on fixed or determinable dates that is recognized as an asset in the creditor's statement of financial position. Examples include but are not limited to accounts receivable (with terms exceeding one year) and notes receivable. This definition encompasses loans accounted for as debt securities.

**Definition 2**

A contractual right to receive money on demand or on fixed or determinable dates that is recognized as an asset in the creditor's statement of financial position. Examples include but are not limited to accounts receivable (with terms exceeding one year) and notes receivable.

**Loan Commitment**

Loan commitments are legally binding commitments to extend credit to a counterparty under certain prespecified terms and conditions. They have fixed expiration dates and may either be fixed-rate or variable-rate. Loan commitments can be either of the following:

- Revolving (in which the amount of the overall line of credit is reestablished upon repayment of previously drawn amounts)
- Nonrevolving (in which the amount of the overall line of credit is not reestablished upon repayment of previously drawn amounts).

Loan commitments can be distributed through syndication arrangements, in which one entity acts as a lead and an agent on behalf of other entities that will each extend credit to a single borrower. Loan commitments generally permit the lender to terminate the arrangement under the terms of covenants negotiated under the agreement. This is not an authoritative or all-encompassing definition.

**Note:** The following definition is Pending Content; see Transition Guidance in 326-10-65-1.
Loan commitments are legally binding commitments to extend credit to a counterparty under certain prespecified terms and conditions. They have fixed expiration dates and may either be fixed-rate or variable-rate. Loan commitments can be either of the following:

- Revolving (in which the amount of the overall commitment is reestablished upon repayment of previously drawn amounts)
- Nonrevolving (in which the amount of the overall commitment is not reestablished upon repayment of previously drawn amounts).

Loan commitments can be distributed through syndication arrangements, in which one entity acts as a lead and an agent on behalf of other entities that will each extend credit to a single borrower. Loan commitments generally permit the lender to terminate the arrangement under the terms of covenants negotiated under the agreement.

**Loan Origination Fees**

Origination fees consist of all of the following:

- Fees that are being charged to the borrower as prepaid interest or to reduce the loan’s nominal interest rate, such as interest buy-downs (explicit yield adjustments)
- Fees to reimburse the lender for origination activities
- Other fees charged to the borrower that relate directly to making the loan (for example, fees that are paid to the lender as compensation for granting a complex loan or agreeing to lend quickly)
- Fees that are not conditional on a loan being granted by the lender that receives the fee but are, in substance, implicit yield adjustments because a loan is granted at rates or terms that would not have otherwise been considered absent the fee (for example, certain syndication fees addressed in paragraph 310-20-25-19)
- Fees charged to the borrower in connection with the process of originating, refinancing, or restructuring a loan. This term includes, but is not limited to, points, management, arrangement, placement, application, underwriting, and other fees pursuant to a lending or leasing transaction and also includes syndication and participation fees to the extent they are associated with the portion of the loan retained by the lender.

**Loan Syndication**

A transaction in which several lenders share in lending to a single borrower. Each lender loans a specific amount to the borrower and has the right to repayment from the borrower. It is common for groups of lenders to jointly fund those loans when the amount borrowed is greater than any one lender is willing to lend.

**Loss Contingency**

An existing condition, situation, or set of circumstances involving uncertainty as to possible loss to an entity that will ultimately be resolved when one or more future events occur or fail to occur. The term loss is used for convenience to include many charges against income that are commonly referred to as expenses and others that are commonly referred to as losses.

**Management**

Persons who are responsible for achieving the objectives of the entity and who have the authority to establish policies and make decisions by which those objectives are to be pursued. Management normally includes members of the board of directors, the chief executive officer, chief operating officer, vice presidents in charge of principal business functions (such as sales, administration, or finance), and other persons who perform similar policy making functions. Persons without formal titles also may be members of management.

**Mandatorily Redeemable Financial Instrument**

Any of various financial instruments issued in the form of shares that embody an unconditional obligation requiring the issuer to redeem the instrument by transferring its assets at a specified or determinable date (or dates) or upon an event that is certain to occur.
Appendix C — Glossary of Selected Terms

ASC 820-10 — Glossary and ASC Master Glossary (continued)

Market Approach
A valuation approach that uses prices and other relevant information generated by market transactions involving identical or comparable (that is, similar) assets, liabilities, or a group of assets and liabilities, such as a business.

Market Participants
Buyers and sellers in the principal (or most advantageous) market for the asset or liability that have all of the following characteristics:
   a. They are independent of each other, that is, they are not related parties, although the price in a related-party transaction may be used as an input to a fair value measurement if the reporting entity has evidence that the transaction was entered into at market terms
   b. They are knowledgeable, having a reasonable understanding about the asset or liability and the transaction using all available information, including information that might be obtained through due diligence efforts that are usual and customary
   c. They are able to enter into a transaction for the asset or liability
   d. They are willing to enter into a transaction for the asset or liability, that is, they are motivated but not forced or otherwise compelled to do so.

Market Risk
The risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises the following:
   a. Interest rate risk
   b. Currency risk
   c. Other price risk.

Market Risk Benefit
Note: The following definition is Pending Content; see Transition Guidance in 944-40-65-2.
A contract or contract feature in a long-term duration contract issued by an insurance entity that both protects the contract holder from other-than-nominal capital market risk and exposes the insurance entity to other-than-nominal capital market risk.

Market-Corroborated Inputs
Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Mining Assets
Mining assets include mineral properties and rights.

Mortgage-Backed Securities
Securities issued by a governmental agency or corporation (for example, Government National Mortgage Association [GNMA] or Federal Home Loan Mortgage Corporation [FHLMC]) or by private issuers (for example, Federal National Mortgage Association [FNMA], banks, and mortgage banking entities). Mortgage-backed securities generally are referred to as mortgage participation certificates or pass-through certificates. A participation certificate represents an undivided interest in a pool of specific mortgage loans. Periodic payments on GNMA participation certificates are backed by the U.S. government. Periodic payments on FHLMC and FNMA certificates are guaranteed by those corporations, but are not backed by the U.S. government.
ASC 820-10 — Glossary and ASC Master Glossary (continued)

**Most Advantageous Market**
The market that maximizes the amount that would be received to sell the asset or minimizes the amount that would be paid to transfer the liability, after taking into account transaction costs and transportation costs.

**Multiemployer Plan**
A pension or postretirement benefit plan to which two or more unrelated employers contribute, usually pursuant to one or more collective-bargaining agreements. A characteristic of multiemployer plans is that assets contributed by one participating employer may be used to provide benefits to employees of other participating employers since assets contributed by an employer are not segregated in a separate account or restricted to provide benefits only to employees of that employer. A multiemployer plan is usually administered by a board of trustees composed of management and labor representatives and may also be referred to as a joint trust or union plan. Generally, many employers participate in a multiemployer plan, and an employer may participate in more than one plan. The employers participating in multiemployer plans usually have a common industry bond, but for some plans the employers are in different industries and the labor union may be their only common bond. Some multiemployer plans do not involve a union. For example, local chapters of a not-for-profit entity (NFP) may participate in a plan established by the related national organization.

**Mutual Entity**
An entity other than an investor-owned entity that provides dividends, lower costs, or other economic benefits directly and proportionately to its owners, members, or participants. Mutual insurance entities, credit unions, and farm and rural electric cooperatives are examples of mutual entities.

**Net Asset Value per Share**
Net asset value per share is the amount of net assets attributable to each share of capital stock (other than senior equity securities, that is, preferred stock) outstanding at the close of the period. It excludes the effects of assuming conversion of outstanding convertible securities, whether or not their conversion would have a diluting effect.

**Net Assets**
The excess or deficiency of assets over liabilities of a not-for-profit-entity, which is divided into two mutually exclusive classes according to the existence or absence of donor-imposed restrictions. See Net Assets with Donor Restrictions and Net Assets without Donor Restrictions.

**Net Assets Available for Benefits**
The difference between a plan’s assets and its liabilities. For purposes of this definition, a plan’s liabilities do not include participants’ accumulated plan benefits.

**Net Assets With Donor Restrictions**
The part of net assets of a not-for-profit entity that is subject to donor-imposed restrictions (donors include other types of contributors, including makers of certain grants).

**Net Assets Without Donor Restrictions**
The part of net assets of a not-for-profit entity that is not subject to donor-imposed restrictions (donors include other types of contributors, including makers of certain grants).

**Net Carrying Amount of Debt**
Net carrying amount of debt is the amount due at maturity, adjusted for unamortized premium, discount, and cost of issuance.
### ASC 820-10 — Glossary and ASC Master Glossary (continued)

**Net Income**
A measure of financial performance resulting from the aggregation of revenues, expenses, gains, and losses that are not items of other comprehensive income. A variety of other terms such as net earnings or earnings may be used to describe net income.

**Net Income Unitrust**
A trust established in connection with a split-interest agreement, in which the donor or a third-party beneficiary receives distributions during the agreement's term of the lesser of the net income earned by the trust or a fixed percentage of the fair value of the trust's assets, with or without recovery and distribution of the shortfall in a subsequent year. Upon termination of the trust, a not-for-profit entity (NFP) receives the assets remaining in the trust.

**Net Investment in an Original Loan**
The net investment in an original loan includes the unpaid loan principal, any remaining unamortized net fees or costs, any remaining unamortized purchase premium or discount, and any accrued interest receivable.

**Net Periodic Pension Cost**
The amount recognized in an employer's financial statements as the cost of a pension plan for a period. Components of net periodic pension cost are service cost, interest cost, actual return on plan assets, gain or loss, amortization of prior service cost or credit, and amortization of the transition asset or obligation existing at the date of initial application of Subtopic 715-30. The term net periodic pension cost is used instead of net pension expense because the service cost component recognized in a period may be capitalized as part of an asset such as inventory.

**Net Periodic Postretirement Benefit Cost**
The amount recognized in an employer's financial statements as the cost of a postretirement benefit plan for a period. Components of net periodic postretirement benefit cost include service cost, interest cost, actual return on plan assets, gain or loss, amortization of prior service cost or credit, and amortization of the transition obligation or asset.

**Network Affiliation Agreement**
A broadcaster may be affiliated with a network under a network affiliation agreement. Under the agreement, the station receives compensation for the network programming that it carries based on a formula designed to compensate the station for advertising sold on a network basis and included in network programming. Program costs, a major expense of television stations, are generally lower for a network affiliate than for an independent station because an affiliate does not incur program costs for network programs.

**New Basis Event**
See Remeasurement Event.

**Noncontrolling Interest**
The portion of equity (net assets) in a subsidiary not attributable, directly or indirectly, to a parent. A noncontrolling interest is sometimes called a minority interest.

**Nonfinancial Asset**
An asset that is not a financial asset. Nonfinancial assets include land, buildings, use of facilities or utilities, materials and supplies, intangible assets, or services.
**Nonmonetary Assets and Liabilities**

Nonmonetary assets and liabilities are assets and liabilities other than monetary ones. Examples are inventories; investments in common stocks; property, plant, and equipment; and liabilities for rent collected in advance.

**Nonperformance Risk**

The risk that an entity will not fulfill an obligation. Nonperformance risk includes, but may not be limited to, the reporting entity's own credit risk.

**Nonpublic Entity**

Any entity that does not meet any of the following conditions:

a. Its debt or equity securities trade in a public market either on a stock exchange (domestic or foreign) or in an over-the-counter market, including securities quoted only locally or regionally.

b. It is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets).

c. It files with a regulatory agency in preparation for the sale of any class of debt or equity securities in a public market.

d. It is required to file or furnish financial statements with the Securities and Exchange Commission.

e. It is controlled by an entity covered by criteria (a) through (d).

**Nonreciprocal Transfer**

**Definition 1**

Nonreciprocal transfer is a transfer of assets or services in one direction, either from an entity to its owners (whether or not in exchange for their ownership interests) or to another entity, or from owners or another entity to the entity. An entity's reacquisition of its outstanding stock is an example of a nonreciprocal transfer.

**Definition 2**

A transaction in which an entity incurs a liability or transfers an asset to another entity (or receives an asset or cancellation of a liability) without directly receiving (or giving) value in exchange.

**Not-for-Profit Entity**

An entity that possesses the following characteristics, in varying degrees, that distinguish it from a business entity:

a. Contributions of significant amounts of resources from resource providers who do not expect commensurate or proportionate pecuniary return

b. Operating purposes other than to provide goods or services at a profit

c. Absence of ownership interests like those of business entities.

Entities that clearly fall outside this definition include the following:

a. All investor-owned entities

b. Entities that provide dividends, lower costs, or other economic benefits directly and proportionately to their owners, members, or participants, such as mutual insurance entities, credit unions, farm and rural electric cooperatives, and employee benefit plans

**Observable Inputs**

Inputs that are developed using market data, such as publicly available information about actual events or transactions, and that reflect the assumptions that market participants would use when pricing the asset or liability.
**One-Time Employee Termination Benefits**
Benefits provided to current employees that are involuntarily terminated under the terms of a one-time benefit arrangement.

**Operating Lease**
From the perspective of a lessee, any lease other than a capital lease.
From the perspective of a lessor, a lease that meets the conditions in paragraph 840-10-25-43(d).

**Note:** The following definition is Pending Content; see Transition Guidance in 842-10-65-1.
From the perspective of a lessee, any lease other than a finance lease.
From the perspective of a lessor, any lease other than a sales-type lease or a direct financing lease.

**Option**
Unless otherwise stated, a call option that gives the holder the right to purchase shares of common stock from the reporting entity in accordance with an agreement upon payment of a specified amount. Options include, but are not limited to, options granted to employees and stock purchase agreements entered into with employees. Options are considered securities. See Call Option.

**Note:** The following definition is Pending Content; see Transition Guidance in 718-10-65-11.
Unless otherwise stated, a call option that gives the holder the right to purchase shares of common stock from the reporting entity in accordance with an agreement upon payment of a specified amount. Options include, but are not limited to, options granted and stock purchase agreements entered into with grantees. Options are considered securities. See Call Option.

**Orderly Transaction**
A transaction that assumes exposure to the market for a period before the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets or liabilities; it is not a forced transaction (for example, a forced liquidation or distress sale).

**Other Comprehensive Income**
Revenues, expenses, gains, and losses that under generally accepted accounting principles (GAAP) are included in comprehensive income but excluded from net income.

**Other Price Risk**
The risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer or by factors affecting all similar financial instruments traded in the market.

**Owners**
Used broadly to include holders of ownership interests (equity interests) of investor-owned entities, mutual entities, or not-for-profit entities. Owners include shareholders, partners, proprietors, or members or participants of mutual entities. Owners also include owner and member interests in the net assets of not-for-profit entities.

**Participating Insurance**
Insurance in which the policyholder is entitled to participate in the earnings or surplus of the insurance entity. The participation occurs through the distribution of dividends to policyholders.
<table>
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<tr>
<th><strong>ASC 820-10 — Glossary and ASC Master Glossary (continued)</strong></th>
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<tr>
<td><strong>Participating Interest</strong></td>
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<td>Paragraph 860-10-40-6A defines the term participating interest.</td>
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**Participation Costs**

Parties involved in the production of a film may be compensated in part by contingent payments based on the financial results of a film pursuant to contractual formulas (participations) and by contingent amounts due under provisions of collective bargaining agreements (residuals). Such parties are collectively referred to as participants, and such costs are collectively referred to as participation costs. Participations may be given to creative talent, such as actors or writers, or to entities from whom distribution rights are licensed.

**Participation Right**

A purchaser’s right under a participating insurance contract to receive future dividends or retroactive rate credits from the insurance entity.

**Performance Indicator**

A performance indicator reports results of operations. A performance indicator and the income from continuing operations reported by for-profit health care entities generally are consistent, except for transactions that clearly are not applicable to one kind of entity (for example, for-profit health care entities typically would not receive contributions, and not-for-profit health care entities would not award stock compensation). That is, a performance indicator is analogous to income from continuing operations of a for-profit entity.

**Perpetual Trust Held by a Third Party**

An arrangement in which a donor establishes and funds a perpetual trust administered by an individual or entity other than the not-for-profit entity (NFP) that is the beneficiary. Under the terms of the trust, the NFP has the irrevocable right to receive the income earned on the trust assets in perpetuity, but never receives the assets held in trust. Distributions received by the NFP may be restricted by the donor.

**Phase**

A contractually or physically distinguishable portion of a real estate project (including time-sharing projects). That portion is distinguishable from other portions based on shared characteristics such as:

- a. Units a developer has declared or legally registered to be for sale
- b. Units linked to an owners association
- c. Units to be constructed during a particular time period
- d. How a developer plans to build the real estate project.

**Physical Settlement**

**Definition 1**

A form of settling a financial instrument under which both of the following conditions are met:

- a. The party designated in the contract as the buyer delivers the full stated amount of cash or other financial instruments to the seller.
- b. The seller delivers the full stated number of shares of stock or other financial instruments or nonfinancial instruments to the buyer.

**Definition 2**

The party designated in the contract as the buyer delivers the full stated amount of cash to the seller, and the seller delivers the full stated number of shares to the buyer.
Plan
An arrangement that is mutually understood by an employer and its employees, whereby an employer undertakes to provide its employees with benefits after they retire in exchange for their services over a specified period of time, upon attaining a specified age while in service, or a combination of both. A plan may be written or it may be implied by a well-defined, although perhaps unwritten, practice of paying postretirement benefits or from oral representations made to current or former employees. See Substantive Plan.

Plan Assets
Definition 1
Assets — usually stocks, bonds, and other investments (except certain insurance contracts as noted in paragraph 715-60-35-109) — that have been segregated and restricted (usually in a trust) to be used for a health and welfare plan (which can include active, terminated, and retired employees or their dependents or beneficiaries). The amount of plan assets includes amounts contributed by the employer, and by plan participants for a contributory plan, and amounts earned from investing the contributions, less benefits, income taxes, and other expenses incurred. Plan assets ordinarily cannot be withdrawn by the employer except under certain circumstances when a plan has assets in excess of obligations and the employer has taken certain steps to satisfy existing obligations. Securities of the employer held by the plan are includable in plan assets provided they are transferable.

Assets not segregated in a trust, or otherwise effectively restricted, so that they cannot be used by the employer for other purposes are not plan assets, even though the employer may intend that those assets be used to provide health and welfare benefits, which may include postretirement benefits. Those assets shall be accounted for in the same manner as other employer assets of a similar nature and with similar restrictions. If a plan has liabilities other than for benefits, those nonbenefit obligations are considered as reductions of plan assets. Amounts accrued by the employer but not yet paid to the plan are not plan assets. If a trust arrangement explicitly provides that segregated assets are available to satisfy claims of creditors in bankruptcy, such a provision would effectively permit those assets to be used for other purposes at the discretion of the employer. It is not necessary to determine that a trust is bankruptcy-proof for the assets of the trust to qualify as plan assets. However, assets held in a trust that explicitly provides that such assets are available to the general creditors of the employer in the event of the employer’s bankruptcy would not qualify as plan assets.

Definition 2
Assets — usually stocks, bonds, and other investments — that have been segregated and restricted, usually in a trust, to provide for pension benefits. The amount of plan assets includes amounts contributed by the employer, and by employees for a contributory plan, and amounts earned from investing the contributions, less benefits paid. Plan assets ordinarily cannot be withdrawn by the employer except under certain circumstances when a plan has assets in excess of obligations and the employer has taken certain steps to satisfy existing obligations. Assets not segregated in a trust or otherwise effectively restricted so that they cannot be used by the employer for other purposes are not plan assets even though it may be intended that such assets be used to provide pensions. If a plan has liabilities other than for benefits, those nonbenefit obligations may be considered as reductions of plan assets. Amounts accrued by the employer but not yet paid to the plan are not plan assets. Securities of the employer held by the plan are includable in plan assets provided they are transferable.

Pooled Income Fund
A trust in which donors are assigned a specific number of units based on the proportion of the fair value of their contributions to the total fair value of the pooled income fund on the date of the donor’s entry to the pooled fund. Until a donor’s death, the donor (or the donor’s designated beneficiary or beneficiaries) is paid the actual income (as defined under the arrangement) earned on the donor’s assigned units. Upon the donor’s death, the value of these assigned units reverts to the NFP.

Postretirement Benefit Plan
See Plan.
**Prepaid Reinsurance Premiums**
Amounts paid to the reinsurer relating to the unexpired portion of reinsured contracts.

**Present Value**
A tool used to link future amounts (cash flows or values) to a present amount using a discount rate (an application of the income approach). Present value techniques differ in how they adjust for risk and in the type of cash flows they use. See Discount Rate Adjustment Technique.

**Primary Beneficiary**
An entity that consolidates a variable interest entity (VIE). See paragraphs 810-10-25-38 through 25-38J for guidance on determining the primary beneficiary.

**Principal Market**
The market with the greatest volume and level of activity for the asset or liability.

**Principal-to-Principal Market**
A market in which transactions, both originations and resales, are negotiated independently with no intermediary. Little information about those transactions may be made available publicly.

**Probable**
The future event or events are likely to occur.

**Probable Reserves**
Probable reserves are reserves for which quantity and grade and/or quality are computed from information similar to that used for proven reserves, but the sites for inspection, sampling, and measurement are farther apart or are otherwise less adequately spaced. The degree of assurance, although lower than that for proven (measured) reserves, is high enough to assume continuity between points of observation.

**Proceeds**
Cash, beneficial interests, servicing assets, derivative instruments, or other assets that are obtained in a transfer of financial assets, less any liabilities incurred.

**Producer**
An individual or an entity that produces and has a financial interest in films for exhibition in movie theaters, on television, or elsewhere.

**Promise to Give**
A written or oral agreement to contribute cash or other assets to another entity. A promise carries rights and obligations — the recipient of a promise to give has a right to expect that the promised assets will be transferred in the future, and the maker has a social and moral obligation, and generally a legal obligation, to make the promised transfer. A promise to give may be either conditional or unconditional.

**Proven Reserves**
Proven reserves are reserves for which both of the following conditions are met:

a. Quantity is computed from dimensions revealed in outcrops, trenches, workings, or drill holes; grade and/or quality are computed from the results of detailed sampling.

b. The sites for inspection, sampling, and measurement are spaced so closely and the geologic character is so well defined that size, shape, depth, and mineral content of reserves are well established.
### Public Business Entity

A public business entity is a business entity meeting any one of the criteria below. Neither a not-for-profit entity nor an employee benefit plan is a business entity.

- It is required by the U.S. Securities and Exchange Commission (SEC) to file or furnish financial statements, or does file or furnish financial statements (including voluntary filers), with the SEC (including other entities whose financial statements or financial information are required to be or are included in a filing).
- It is required by the Securities Exchange Act of 1934 (the Act), as amended, or rules or regulations promulgated under the Act, to file or furnish financial statements with a regulatory agency other than the SEC.
- It is required to file or furnish financial statements with a foreign or domestic regulatory agency in preparation for the sale of or for purposes of issuing securities that are not subject to contractual restrictions on transfer.
- It has issued, or is a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market.
- It has one or more securities that are not subject to contractual restrictions on transfer, and it is required by law, contract, or regulation to prepare U.S. GAAP financial statements (including notes) and make them publicly available on a periodic basis (for example, interim or annual periods). An entity must meet both of these conditions to meet this criterion.

An entity may meet the definition of a public business entity solely because its financial statements or financial information is included in another entity's filing with the SEC. In that case, the entity is only a public business entity for purposes of financial statements that are filed or furnished with the SEC.

### Publicly Traded Company

A publicly traded company includes any company whose securities trade in a public market on either of the following:

- A stock exchange (domestic or foreign)
- In the over-the-counter market (including securities quoted only locally or regionally), or any company that is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets).

Additionally, when a company is required to file or furnish financial statements with the SEC or makes a filing with a regulatory agency in preparation for sale of its securities in a public market it is considered a publicly traded company for this purpose.

Conduit debt securities refers to certain limited-obligation revenue bonds, certificates of participation, or similar debt instruments issued by a state or local governmental entity for the express purpose of providing financing for a specific third party (the conduit bond obligor) that is not a part of the state or local government's financial reporting entity. Although conduit debt securities bear the name of the governmental entity that issues them, the governmental entity often has no obligation for such debt beyond the resources provided by a lease or loan agreement with the third party on whose behalf the securities are issued. Further, the conduit bond obligor is responsible for any future financial reporting requirements.

### Purchased Call Option

A contract that allows the reporting entity to buy a specified quantity of its own stock from the writer of the contract at a fixed price for a given period. See Call Option.
**Purchased Financial Assets With Credit Deterioration**

**Note:** The following definition is Pending Content; see Transition Guidance in 326-10-65-1.

Acquired individual financial assets (or acquired groups of financial assets with similar risk characteristics) that as of the date of acquisition have experienced a more-than-insignificant deterioration in credit quality since origination, as determined by an acquirer’s assessment. See paragraph 326-20-55-5 for more information on the meaning of similar risk characteristics for assets measured on an amortized cost basis.

**Pushdown Accounting**

Use of the acquirer’s basis in the preparation of the acquiree’s separate financial statements.

**Rabbi Trusts**

Rabbi trusts are grantor trusts generally set up to fund compensation for a select group of management or highly paid executives. To qualify as a rabbi trust for income tax purposes, the terms of the trust agreement must explicitly state that the assets of the trust are available to satisfy the claims of general creditors in the event of bankruptcy of the employer.

**Reacquisition Price of Debt**

The amount paid on extinguishment, including a call premium and miscellaneous costs of reacquisition. If extinguishment is achieved by a direct exchange of new securities, the reacquisition price is the total present value of the new securities.

**Readily Determinable Fair Value**

An equity security has a readily determinable fair value if it meets any of the following conditions:

a. The fair value of an equity security is readily determinable if sales prices or bid-and-asked quotations are currently available on a securities exchange registered with the U.S. Securities and Exchange Commission (SEC) or in the over-the-counter market, provided that those prices or quotations for the over-the-counter market are publicly reported by the National Association of Securities Dealers Automated Quotations systems or by OTC Markets Group Inc. Restricted stock meets that definition if the restriction terminates within one year.

b. The fair value of an equity security traded only in a foreign market is readily determinable if that foreign market is of a breadth and scope comparable to one of the U.S. markets referred to above.

c. The fair value of an equity security that is an investment in a mutual fund or in a structure similar to a mutual fund (that is, a limited partnership or a venture capital entity) is readily determinable if the fair value per share (unit) is determined and published and is the basis for current transactions.

**Recipient Entity**

A not-for-profit entity (NFP) or charitable trust that accepts assets from a donor or other resource provider and agrees to use those assets on behalf of or transfer those assets, the return on investment of those assets, or both to a beneficiary that is specified by the donor or resource provider.

**Reinsurance**

A transaction in which a reinsurer (assuming entity), for a consideration (premium), assumes all or part of a risk undertaken originally by another insurer (ceding entity). For indemnity reinsurance, the legal rights of the insured are not affected by the reinsurance transaction and the insurance entity issuing the insurance contract remains liable to the insured for payment of policy benefits. Assumption or novation reinsurance contracts that are legal replacements of one insurer by another extinguish the ceding entity’s liability to the policyholder.

**Reinsurance Recoverable**

All amounts recoverable from reinsurers for paid and unpaid claims and claim settlement expenses, including estimated amounts receivable for unsettled claims, claims incurred but not reported, or policy benefits.
Related Parties
Related parties include:

a. Affiliates of the entity
b. Entities for which investments in their equity securities would be required, absent the election of the fair value option under the Fair Value Option Subsection of Section 825-10-15, to be accounted for by the equity method by the investing entity
c. Trusts for the benefit of employees, such as pension and profit-sharing trusts that are managed by or under the trusteeship of management
d. Principal owners of the entity and members of their immediate families
e. Management of the entity and members of their immediate families
f. Other parties with which the entity may deal if one party controls or can significantly influence the management or operating policies of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interests
g. Other parties that can significantly influence the management or operating policies of the transacting parties or that have an ownership interest in one of the transacting parties and can significantly influence the other to an extent that one or more of the transacting parties might be prevented from fully pursuing its own separate interests.

Remainder Interest
The right to receive all or a portion of the assets of a split-interest agreement remaining at the end of the agreement’s term.

Remeasurement Event
A remeasurement (new basis) event is an event identified in other authoritative accounting literature, other than the recognition of an other-than-temporary impairment, that requires a financial instrument to be remeasured to its fair value at the time of the event but does not require that financial instrument to be reported at fair value continually with the change in fair value recognized in earnings. Examples of remeasurement events are business combinations and significant modifications of debt as discussed in paragraph 470-50-40-6.

Note: The following definition is Pending Content; see Transition Guidance in 326-10-65-1

A remeasurement (new basis) event is an event identified in other authoritative accounting literature, other than the measurement of an impairment under Topic 321 or credit loss under Topic 326, that requires a financial instrument to be remeasured to its fair value at the time of the event but does not require that financial instrument to be reported at fair value continually with the change in fair value recognized in earnings. Examples of remeasurement events are business combinations and significant modifications of debt as discussed in paragraph 470-50-40-6.

Reporting Entity
An entity or group whose financial statements are being referred to. Those financial statements reflect any of the following:

a. The financial statements of one or more foreign operations by combination, consolidation, or equity accounting
b. Foreign currency transactions.
Repurchase Agreement
An agreement under which the transferor (repo party) transfers a financial asset to a transferee (repo counterparty or reverse party) in exchange for cash and concurrently agrees to reacquire that financial asset at a future date for an amount equal to the cash exchanged plus or minus a stipulated interest factor. Instead of cash, other securities or letters of credit sometimes are exchanged. Some repurchase agreements call for repurchase of financial assets that need not be identical to the financial assets transferred.

Research and Development
Research is planned search or critical investigation aimed at discovery of new knowledge with the hope that such knowledge will be useful in developing a new product or service (referred to as product) or a new process or technique (referred to as process) or in bringing about a significant improvement to an existing product or process.

Development is the translation of research findings or other knowledge into a plan or design for a new product or process or for a significant improvement to an existing product or process whether intended for sale or use. It includes the conceptual formulation, design, and testing of product alternatives, construction of prototypes, and operation of pilot plants.

Residual Value
The estimated fair value of an intangible asset at the end of its useful life to an entity, less any disposal costs.

Revenue
Inflows or other enhancements of assets of an entity or settlements of its liabilities (or a combination of both) from delivering or producing goods, rendering services, or other activities that constitute the entity's ongoing major or central operations.

Reverse Acquisition
An acquisition in which the entity that issues securities (the legal acquirer) is identified as the acquiree for accounting purposes based on the guidance in paragraphs 805-10-55-11 through 55-15. The entity whose equity interests are acquired (the legal acquiree) must be the acquirer for accounting purposes for the transaction to be considered a reverse acquisition.

Risk Premium
Compensation sought by risk-averse market participants for bearing the uncertainty inherent in the cash flows of an asset or a liability. Also referred to as a risk adjustment.

Sales-Type Lease
From the perspective of a lessor, a lease that meets either of the conditions in paragraph 840-10-25-43(a).

Note: The following definition is Pending Content; see Transition Guidance in 842-10-65-1.

From the perspective of a lessor, a lease that meets one or more of the criteria in paragraph 842-10-25-2.

Securitization
The process by which financial assets are transformed into securities.
### Security
A share, participation, or other interest in property or in an entity of the issuer or an obligation of the issuer that has all of the following characteristics:

- **a.** It is either represented by an instrument issued in bearer or registered form or, if not represented by an instrument, is registered in books maintained to record transfers by or on behalf of the issuer.
- **b.** It is of a type commonly dealt in on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment.
- **c.** It either is one of a class or series or by its terms is divisible into a class or series of shares, participations, interests, or obligations.

### Separate Account

#### Definition 1
A special account established by an insurance entity solely for the purpose of investing the assets of one or more plans. Funds in a separate account are not commingled with other assets of the insurance entity for investment purposes.

#### Definition 2
A separate investment account established and maintained by an insurance entity under relevant state insurance law to which funds have been allocated for certain contracts of the insurance entity or similar accounts used for foreign originated products. The term separate accounts includes separate accounts and subaccounts or investment divisions of separate accounts.

### Separate Account Arrangement
An arrangement under which all or a portion of a contract holder’s funds is allocated to a specific separate account maintained by the insurance entity.

### Servicing Assets
A contract to service financial assets under which the benefits of servicing are expected to more than adequately compensate the servicer for performing the servicing. A servicing contract is either:

- **a.** Undertaken in conjunction with selling or securitizing the financial assets being serviced
- **b.** Purchased or assumed separately.

### Servicing Liabilities
A contract to service financial assets under which the estimated future revenues from contractually specified servicing fees, late charges, and other ancillary revenues (benefits of servicing) are not expected to adequately compensate the servicer for performing the servicing.

### Shares
Shares includes various forms of ownership that may not take the legal form of securities (for example, partnership interests), as well as other interests, including those that are liabilities in substance but not in form. (Business entities have interest holders that are commonly known by specialized names, such as stockholders, partners, and proprietors, and by more general names, such as investors, but all are encompassed by the descriptive term owners. Equity of business entities is, thus, commonly known by several names, such as owners’ equity, stockholders’ equity, ownership, equity capital, partners’ capital, and proprietorship. Some entities [for example, mutual organizations] do not have stockholders, partners, or proprietors in the usual sense of those terms but do have participants whose interests are essentially ownership interests, residual interests, or both.)
### ASC 820-10 — Glossary and ASC Master Glossary (continued)

**Significant Influence**
Paragraphs 323-10-15-6 through 15-11 define significant influence.

**Spinoff**
The transfer of assets that constitute a business by an entity (the spinnor) into a new legal spun-off entity (the spinnee), followed by a distribution of the shares of the spinnee to its shareholders, without the surrender by the shareholders of any stock of the spinnor.

**Split-Interest Agreement**
An agreement in which a donor enters into a trust or other arrangement under which a not-for-profit entity (NFP) receives benefits that are shared with other beneficiaries. A typical split-interest agreement has the following two components:
   a. A lead interest
   b. A remainder interest.

**Split-off**
A transaction in which a parent entity exchanges its stock in a subsidiary for parent entity stock held by its shareholders.

**Sponsor**
In the case of a pension plan established or maintained by a single employer, the employer; in the case of a plan established or maintained by an employee entity, the employee entity; in the case of a plan established or maintained jointly by two or more employers or by one or more employers and one or more employee entities, the association, committee, joint board of trustees, or other group of representatives of the parties that have established or that maintain the pension plan.

**Standalone Selling Price**
The price at which an entity would sell a promised good or service separately to a customer.

**Stock Dividend**
An issuance by a corporation of its own common shares to its common shareholders without consideration and under conditions indicating that such action is prompted mainly by a desire to give the recipient shareholders some ostensibly separate evidence of a part of their respective interests in accumulated corporate earnings without distribution of cash or other property that the board of directors deems necessary or desirable to retain in the business. A stock dividend takes nothing from the property of the corporation and adds nothing to the interests of the stockholders; that is, the corporation's property is not diminished and the interests of the stockholders are not increased. The proportional interest of each shareholder remains the same.

**Structured Note**
A debt instrument whose cash flows are linked to the movement in one or more indexes, interest rates, foreign exchange rates, commodities prices, prepayment rates, or other market variables. Structured notes are issued by U.S. government-sponsored enterprises, multilateral development banks, municipalities, and private entities. The notes typically contain embedded (but not separable or detachable) forward components or option components such as caps, calls, and floors. Contractual cash flows for principal, interest, or both can vary in amount and timing throughout the life of the note based on nontraditional indexes or nontraditional uses of traditional interest rates or indexes.
Appendix C — Glossary of Selected Terms

ASC 820-10 — Glossary and ASC Master Glossary (continued)

Sublease
A transaction in which a leased property is re-leased by the original lessee to a third party, and the lease agreement between the two original parties remains in effect.

Note: The following definition is Pending Content; see Transition Guidance in 842-10-65-1.

A transaction in which an underlying asset is re-leased by the lessee (or intermediate lessor) to a third party (the sublessee) and the original (or head) lease between the lessor and the lessee remains in effect.

Subsidiary
An entity, including an unincorporated entity such as a partnership or trust, in which another entity, known as its parent, holds a controlling financial interest. (Also, a variable interest entity that is consolidated by a primary beneficiary.)

Substantive Plan
The terms of the postretirement benefit plan as understood by an employer that provides postretirement benefits and the employees who render services in exchange for those benefits. The substantive plan is the basis for the accounting for that exchange transaction. In some situations an employer’s cost-sharing policy, as evidenced by past practice or by communication of intended changes to a plan’s cost-sharing provisions, or a past practice of regular increases in certain monetary benefits, may indicate that the substantive plan differs from the extant written plan.

Systematic Risk
The common risk shared by an asset or a liability with the other items in a diversified portfolio. Portfolio theory holds that in a market in equilibrium, market participants will be compensated only for bearing the systematic risk inherent in the cash flows. (In markets that are inefficient or out of equilibrium, other forms of return or compensation might be available.) Also referred to as nondiversifiable risk.

Trading
An activity involving securities sold in the near term and held for only a short period of time. The term trading contemplates a holding period generally measured in hours and days rather than months or years. See paragraph 948-310-40-1 for clarification of the term trading for a mortgage banking entity.

Trading Purposes
The determination of what constitutes trading purposes is based on the intent of the issuer or holder and shall be consistent with the definition of trading in paragraph 320-10-25-1(a).

Trading Securities
Securities that are bought and held principally for the purpose of selling them in the near term and therefore held for only a short period of time. Trading generally reflects active and frequent buying and selling, and trading securities are generally used with the objective of generating profits on short-term differences in price.

Transaction Costs
The costs to sell an asset or transfer a liability in the principal (or most advantageous) market for the asset or liability that are directly attributable to the disposal of the asset or the transfer of the liability and meet both of the following criteria:

a. They result from and are essential to that transaction

b. They would not have been incurred by the entity had the decision to sell the asset or transfer the liability not been made (similar to costs to sell, as defined in paragraph 360-10-35-38).
Transaction Price
The amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties.

Transfer
Definition 1
The term transfer is used in a broad sense consistent with its use in FASB Concepts Statement No. 6, Elements of Financial Statements (such as in paragraph 137), rather than in the narrow sense in which it is used in Subtopic 860-10.

Definition 2
The conveyance of a noncash financial asset by and to someone other than the issuer of that financial asset.

A transfer includes the following:
   a. Selling a receivable
   b. Putting a receivable into a securitization trust
   c. Posting a receivable as collateral.

A transfer excludes the following:
   a. The origination of a receivable
   b. Settlement of a receivable
   c. The restructuring of a receivable into a security in a troubled debt restructuring.

Transferee
An entity that receives a financial asset, an interest in a financial asset, or a group of financial assets from a transferor.

Transferor
An entity that transfers a financial asset, an interest in a financial asset, or a group of financial assets that it controls to another entity.

Transferred Financial Assets
Transfers of any of the following:
   a. An entire financial asset
   b. A group of entire financial assets
   c. A participating interest in an entire financial asset.

Transportation Costs
The costs that would be incurred to transport an asset from its current location to its principal (or most advantageous) market.

Troubled Debt Restructuring
A restructuring of a debt constitutes a troubled debt restructuring if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider.
Trustee

**Definition 1**
A person appointed by the Bankruptcy Court in certain situations based on the facts of the case, not related to the size of the entity or the amount of unsecured debt outstanding, at the request of a party in interest after a notice and hearing.

**Definition 2**
An entity that has a duty to hold and manage assets for the benefit of a specified beneficiary in accordance with a charitable trust agreement. In some states, not-for-profit entities (NFPs) are organized under trust law rather than as corporations. Those NFPs are not trustees as defined because, under those statutes, they hold assets in trust for the community or some other broadly described group, rather than for a specific beneficiary.

**Unallocated Contract**
A contract with an insurance entity under which payments to the insurance entity are accumulated in an unallocated fund (not allocated to specific plan participants) to be used either directly or through the purchase of annuities, to meet benefit payments when employees retire. Funds held by the insurance entity under an unallocated contract may be withdrawn and otherwise invested.

**Uncommitted Loans**
A mortgage loan that does not meet the specific terms of a commitment or for which a reasonable doubt exists about the acceptance of the loan under a commitment.

**Unconditional Promise to Give**
A promise to give that depends only on passage of time or demand by the promisee for performance.

**Underlying**
A specified interest rate, security price, commodity price, foreign exchange rate, index of prices or rates, or other variable (including the occurrence or nonoccurrence of a specified event such as a scheduled payment under a contract). An underlying may be a price or rate of an asset or liability but is not the asset or liability itself. An underlying is a variable that, along with either a notional amount or a payment provision, determines the settlement of a derivative instrument.

**Underlying Asset**
*Note:* The following definition is Pending Content; see Transition Guidance in 842-10-65-1.
An asset that is the subject of a lease for which a right to use that asset has been conveyed to a lessee. The underlying asset could be a physically distinct portion of a single asset.

**Unit of Account**
The level at which an asset or a liability is aggregated or disaggregated in a Topic for recognition purposes.

**Unobservable Inputs**
Inputs for which market data are not available and that are developed using the best information available about the assumptions that market participants would use when pricing the asset or liability.

**Unsystematic Risk**
The risk specific to a particular asset or liability. Also referred to as diversifiable risk.
ASC 820-10 — Glossary and ASC Master Glossary (continued)

Value Beyond Proven and Probable Reserves
Value beyond proven and probable reserves is the economic value that exists in a mining asset beyond the value attributable to proven and probable reserves. The distinction between the categories of reserves relates to the level of geological evidence and, therefore, confidence in the reserve estimates.

Variable Interest Entity
A legal entity subject to consolidation according to the provisions of the Variable Interest Entities Subsections of Subtopic 810-10.

Voluntary Health and Welfare Entity
A not-for-profit entity (NFP) that is formed for the purpose of performing voluntary services for various segments of society and that is tax exempt (organized for the benefit of the public), supported by the public, and operated on a not-for-profit basis. Most voluntary health and welfare entities concentrate their efforts and expend their resources in an attempt to solve health and welfare problems of our society and, in many cases, those of specific individuals. As a group, voluntary health and welfare entities include those NFPs that derive their revenue primarily from voluntary contributions from the general public to be used for general or specific purposes connected with health, welfare, or community services. For purposes of this definition, the general public excludes governmental entities when determining whether an NFP is a voluntary health and welfare entity.

Warranty
A guarantee for which the underlying is related to the performance (regarding function, not price) of nonfinancial assets that are owned by the guaranteed party. The obligation may be incurred in connection with the sale of goods or services; if so, it may require further performance by the seller after the sale has taken place.
Appendix D — Titles of Standards and Other Literature

**AICPA Literature**

**Accounting and Valuation Guides**

*Assets Acquired in a Business Combination to Be Used in Research and Development Activities*

*Testing Goodwill for Impairment*

*Valuation of Privately-Held-Company Equity Securities Issued as Compensation*

**Industry Audit Guides**

*Audits of Voluntary Health and Welfare Organizations*

*Investment Companies*

**Technical Questions and Answers**

Section 6910.34, “Application of the Notion of Value Maximization for Measuring Fair Value of Debt and Controlling Equity Positions”

Section 6910.35, “Assessing Control When Measuring Fair Value”

**U.S. Clarified Auditing Standards**

AU-C Section 540, “Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures”

**EITF Literature**


**FASB Literature**

**ASC Topics**

ASC 105, *Generally Accepted Accounting Principles*

ASC 205, *Presentation of Financial Statements*

ASC 210, *Balance Sheet*

ASC 220, *Income Statement — Reporting Comprehensive Income*

ASC 230, *Statement of Cash Flows*
ASC 235, Notes to Financial Statements
ASC 250, Accounting Changes and Error Corrections
ASC 260, Earnings per Share
ASC 270, Interim Reporting
ASC 280, Segment Reporting
ASC 310, Receivables
ASC 320, Investments — Debt and Equity Securities
ASC 321, Investments — Equity Securities
ASC 323, Investments — Equity Method and Joint Ventures
ASC 325, Investments — Other
ASC 326, Financial Instruments — Credit Losses
ASC 330, Inventory
ASC 350, Intangibles — Goodwill and Other
ASC 360, Property, Plant, and Equipment
ASC 405, Liabilities
ASC 410, Asset Retirement and Environmental Obligations
ASC 420, Exit or Disposal Cost Obligations
ASC 440, Commitments
ASC 450, Contingencies
ASC 460, Guarantees
ASC 470, Debt
ASC 480, Distinguishing Liabilities From Equity
ASC 505, Equity
ASC 606, Revenue From Contracts With Customers
ASC 610, Other Income
ASC 710, Compensation — General
ASC 712, Compensation — Nonretirement Postemployment Benefits
ASC 715, Compensation — Retirement Benefits
ASC 718, Compensation — Stock Compensation
ASC 720, Other Expenses
ASC 730, Research and Development
ASC 740, Income Taxes
ASC 805, Business Combinations
Appendix D — Titles of Standards and Other Literature

ASC 810, Consolidation
ASC 815, Derivatives and Hedging
ASC 820, Fair Value Measurement
ASC 825, Financial Instruments
ASC 830, Foreign Currency Matters
ASC 835, Interest
ASC 840, Leases
ASC 842, Leases
ASC 845, Nonmonetary Transactions
ASC 850, Related Party Disclosures
ASC 852, Reorganizations
ASC 855, Subsequent Events
ASC 860, Transfers and Servicing
ASC 920, Entertainment — Broadcasters
ASC 926, Entertainment — Films
ASC 930, Extractive Activities — Mining
ASC 932, Extractive Activities — Oil and Gas
ASC 940, Financial Services — Brokers and Dealers
ASC 942, Financial Services — Depository and Lending
ASC 944, Financial Services — Insurance
ASC 946, Financial Services — Investment Companies
ASC 948, Financial Services — Mortgage Banking
ASC 950, Financial Services — Title Plant
ASC 952, Franchisors
ASC 954, Health Care Entities
ASC 958, Not-for-Profit Entities
ASC 960, Plan Accounting — Defined Benefit Pension Plans
ASC 962, Plan Accounting — Defined Contribution Pension Plans
ASC 965, Plan Accounting — Health and Welfare Benefit Plans
ASC 970, Real Estate — General
ASC 972, Real Estate — Common Interest Realty Associations

ASC 974, Real Estate — Real Estate Investment Trusts

ASC 985, Software

**ASUs**

ASU 2009-05, Fair Value Measurements and Disclosures (Topic 820): Measuring Liabilities at Fair Value

ASU 2009-12, Fair Value Measurements and Disclosures (Topic 820): Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)

ASU 2009-16, Fair Value Measurements and Disclosures (Topic 820): Accounting for Transfers of Financial Assets

ASU 2010-06, Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures About Fair Value Measurements

ASU 2010-28, Intangibles — Goodwill and Other (Topic 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units With Zero or Negative Carrying Amounts

ASU 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs

ASU 2012-04, Technical Corrections and Improvements

ASU 2012-07, Entertainment — Films (Topic 926): Accounting for Fair Value Information That Arises After the Measurement Date and Its Inclusion in the Impairment Analysis of Unamortized Film Costs

ASU 2013-03, Financial Instruments (Topic 825): Clarifying the Scope and Applicability of a Particular Disclosure to Nonpublic Entities

ASU 2013-09, Fair Value Measurement (Topic 820): Deferral of the Effective Date of Certain Disclosures for Nonpublic Employee Benefit Plans in Update No. 2011-04


ASU 2015-07, Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent) — a consensus of the FASB Emerging Issues Task Force

ASU 2015-10, Technical Corrections and Improvements


ASU 2016-02, Leases (Topic 842)

ASU 2016-13, Financial Instruments — Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments

ASU 2016-19, Technical Corrections and Improvements

ASU 2017-04, Intangibles — Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment


ASU 2018-05, Income Taxes (Topic 740): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118
ASU 2018-07, Compensation — Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting

ASU 2018-09, Codification Improvements


ASU 2019-01, Leases (Topic 842): Codification Improvements

ASU 2019-04, Codification Improvements to Topic 326, Financial Instruments — Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments

ASU 2019-05, Financial Instruments — Credit Losses (Topic 326): Targeted Transition Relief

ASU 2019-06, Intangibles — Goodwill and Other (Topic 350), Business Combinations (Topic 805), and Not-for-Profit Entities (Topic 958): Extending the Private Company Accounting Alternatives on Goodwill and Certain Identifiable Intangible Assets to Not-for-Profit Entities

**Concepts Statements**

No. 6, Elements of Financial Statements

No. 7, Using Cash Flow Information and Present Value in Accounting Measurements

**International Standards**

IFRS 9, Financial Instruments

IFRS 13, Fair Value Measurement

**PCAOB Literature**

**Auditing Standards**

AS 11, “Consideration of Materiality in Planning and Performing an Audit”

AU Section 328, Auditing Fair Value Measurements and Disclosures

**SEC Literature**

**Accounting Series Release (ASR)**

No. 118 (FRR Section 404), Registered Investment Companies

**Financial Reporting Manual (FRM)**

Topic No. 2, “Other Financial Statements Required”

Topic No. 9, “Management’s Discussion and Analysis of Financial Position and Results of Operations (MD&A)”

**Regulation S-K**

Item 303, “Management’s Discussion and Analysis of Financial Condition and Results of Operations”
**Regulation S-X**

Rule 3-09, “Separate Financial Statements of Subsidiaries Not Consolidated and 50 Percent or Less Owned Persons”

Rule 4-08(g), “General Notes to Financial Statements; Summarized Financial Information of Subsidiaries Not Consolidated and 50 Percent or Less Owned Persons”

**SAB Topics**

No. 1.M, “Materiality”

No. 5.S, “Quasi-Reorganization”

**Superseded Literature**

**EITF Issues**

No. 97-14, “Accounting for Deferred Compensation Arrangements Where Amounts Earned Are Held in a Rabbi Trust and Invested”

No. 98-1, “Valuation of Debt Assumed in a Purchase Business Combination”

No. 02-3, “Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities”

**FASB Staff Positions (FSPs)**

FSP FAS 132(R)-1, *Employers’ Disclosures About Postretirement Benefit Plan Assets*

FSP FAS 157-1, *Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement Under Statement 13*

FSP FAS 157-2, *Effective Date of FASB Statement No. 157*

FSP FAS 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active*

FSP FAS 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*

**FASB Statements**

No. 107, *Disclosures About Fair Value of Financial Instruments*

No. 155, *Accounting for Certain Hybrid Financial Instruments* — an amendment of FASB Statements No. 133 and 140

No. 157, *Fair Value Measurements*

No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*
### Appendix E — Abbreviations

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>AICPA</td>
<td>American Institute of Certified Public Accountants</td>
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<tr>
<td>AOIC</td>
<td>accumulated other comprehensive income</td>
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<td>APIC</td>
<td>additional paid-in capital</td>
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<td>ARO</td>
<td>asset retirement obligation</td>
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<tr>
<td>ASC</td>
<td>Accounting Standards Codification</td>
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<td>ASU</td>
<td>Accounting Standards Update</td>
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<tr>
<td>CD</td>
<td>certificate of deposit</td>
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<tr>
<td>CFE</td>
<td>collateralized financing entity</td>
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<td>CSV</td>
<td>cash surrender value</td>
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<td>CVA</td>
<td>credit valuation adjustment</td>
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<td>CUSIP</td>
<td>Committee on Uniform Securities Identification Procedures</td>
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<tr>
<td>EBITDA</td>
<td>earnings before income taxes, depreciation, and amortization</td>
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<td>EITF</td>
<td>FASB Emerging Issues Task Force</td>
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<td>EPD</td>
<td>early payment default</td>
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<td>EPS</td>
<td>earnings per share</td>
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<td>ESOP</td>
<td>employee stock ownership plan</td>
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<td>FASB</td>
<td>Financial Accounting Standards Board</td>
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<td>FBRIC</td>
<td>fully benefit-responsive investment contract</td>
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<td>FRM</td>
<td>SEC Division of Corporation Finance's Financial Reporting Manual</td>
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<td>FVO</td>
<td>fair value option</td>
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<td>GAAP</td>
<td>generally accepted accounting principles</td>
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<th>Abbreviation</th>
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<td>GP</td>
<td>general partner</td>
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<td>HFI</td>
<td>held for investment</td>
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<td>HFS</td>
<td>held for sale</td>
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<td>HKEx</td>
<td>Hong Kong Exchange</td>
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<td>IASB</td>
<td>International Accounting Standards Board</td>
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<td>ICFR</td>
<td>internal control over financial reporting</td>
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<tr>
<td>IFRS</td>
<td>International Financial Reporting Standard</td>
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<td>IPO</td>
<td>initial public offering</td>
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<td>LIBOR</td>
<td>London Interbank Offered Rate</td>
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<td>LP</td>
<td>limited partner</td>
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<tr>
<td>M&amp;A</td>
<td>mergers and acquisitions</td>
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<td>MD&amp;A</td>
<td>Management's Discussion and Analysis</td>
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<tr>
<td>MMBtu</td>
<td>million Btu</td>
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<tr>
<td>MW</td>
<td>megawatts</td>
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<td>NASDAQ</td>
<td>National Association of Securities Dealers Automated Quotations</td>
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<td>NAV</td>
<td>net asset value</td>
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<tr>
<td>NFP</td>
<td>not for profit</td>
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<td>NYSE</td>
<td>New York Stock Exchange</td>
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<td>OCA</td>
<td>SEC Office of the Chief Accountant</td>
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<td>OCI</td>
<td>other comprehensive income</td>
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<td>OTC</td>
<td>over the counter</td>
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<tr>
<td>PCAOB</td>
<td>Public Company Accounting Oversight Board</td>
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<tr>
<td>PP&amp;E</td>
<td>property, plant, and equipment</td>
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<td>Abbreviation</td>
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<tr>
<td>RMBS</td>
<td>residential mortgage-backed security</td>
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<td>SEC</td>
<td>Securities and Exchange Commission</td>
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<tr>
<td>TAB</td>
<td>tax amortization benefits</td>
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<tr>
<td>VIE</td>
<td>variable interest entity</td>
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