On the Accounting Horizon

Bankers Conference
October 1, 2009

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Disclaimer

The contents of this presentation and views presented today are my own and do not reflect the views or policy of the Federal Reserve Bank of Boston, Federal Reserve Board or Federal Reserve System
Reminder

“The first commandment is: Thou shalt not shoot the messenger.”
Overview

- Fair Value Accounting
- Off-Balance Sheet Accounting
- Financial Statement Presentation
- International Financial Reporting Standards
Fair Value Accounting
Motivation for Change

- Evolution of GAAP
  - Asset/Liability recognition model
  - Increase transparency, reduce complexity
  - Guidance to address specific issues (business combinations, derivatives and impairment accounting)
  - Convergence with IASB
Fair Value Accounting

Debate

- Fair value is a more relevant measure for financial instruments providing investors with more transparent, timely and accurate information.
- The current mixed cost measurement model hides or delays the disclosure of important information which produces inefficient market decisions.
- A company should be presented as an investment in a collection of assets and liabilities and priced based on net asset value.
Fair Value Accounting

Debate

- Fair value can be **unreliable** when markets are illiquid or distressed
- Application of fair value has had unintended consequences
- Assets and liabilities should be presented in terms of a going concern and emphasis placed on realizable returns
Fair Value Accounting

On the Horizon

- Agreement among all standard setters that Fair Value is the only long-term solution to simplify accounting
- Exposure Draft coming in Q1 2010 to recommend that all loans and investment securities including Held-to-Maturity be measured at fair value
- IASB document calling for fair value measurement for all financial instruments except for those with basic loan features that are managed on a contractual yield basis
Off Balance Sheet Accounting
Motivation for Change

- Abuse of Special Purpose Entities
- Sarbanes Oxley - SEC Report to Congress
- Financial/Subprime Crisis
Off Balance Sheet Accounting
Coming Back On

- Pension Accounting – FAS 158
- Contingencies - FIN 48, FAS 141(r)
- Securitizations and participations – FAS 166
- Off Balance Sheet Entities (SPEs) – FAS 167
- Lease accounting project
Off Balance Sheet Accounting
On the Horizon

- Lease Accounting Project
- Discussion Paper – Lessees must account for their right to use a leased item as an asset and their obligation to pay future rental installments for that item as a liability

Implications for Banks
- Balance sheet impacts for operating leases
- Possible impact to lessor business models
- Lessor accounting to be addressed in next round of changes

10/8/2009
Financial Statement Presentation

Motivation for Change

- A desire to disaggregate recurring from non recurring activity
- A need for better information to project cash flows
- Looking to address questions about the relevance of Net Income and Comprehensive Income
Financial Statement Presentation

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- Joint project with the IASB to revamp the organization and presentation of financial statements
- Three phase project began in 2004
- Phase A – Completed deliberations and issued tentative conclusions in 2007
- Phase B - Discussion Papers issued in October 2008 with 227 comments received
- Phase C – Goal to issue standards by June 30, 2011
Financial Statements should be cohesive at the line-item level

Classifications would be based on functional activities similar to cash flow statement

Total Assets/Liabilities, Net Income and Extraordinary Items would be eliminated
International Financial Reporting Standards

Motivating Factors

- Global nature of financial markets
- Push for increased transparency and consistency
- Over 100 countries adopted or moving toward adoption of IFRS
International Financial Reporting Standards
Convergence or Conversion?

- **Convergence** - The development of high quality, compatible accounting standards that could be used for both domestic and cross-border financial reporting achieved through (1) short-term projects to eliminate narrow differences between similar standards, (2) joint long-term projects to develop common standards, and (3) coordinating future technical agendas.
International Financial Reporting Standards
On the Horizon

2002
FASB and IASB MOU to coordinate work and make existing standards compatible

2007
SEC eliminates the US GAAP reconciliation requirement

2005
100 Countries including the EU require or permit the use of IFRS

2009
G-20 and US Treasury recommend development of single set of global standards

???
Convergence or Conversion or None of the Above
Questions or Comments?