Interpretation of the Emerging Accounting Issues Working Group

INT 09-04: Application of the Fair Value Definition

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INT 09-04 Dates Discussed

March 26, 2009; April 7, 2009; April 16, 2009; June 13, 2009

INT 09-04 References

Fair Value Definition in the Glossary to the *Accounting Practices and Procedures Manual*

INT 09-04 Issue

1. The accounting issue is application of the current definition of "fair value" within the

6. Each reporting entity shall use its judgment in determining whether the there has been a significant decrease in the volume and level of activity for the asset or liability when compared with normal market activity for the asset or liability. This list of example factors is not considered all-inclusive, and any or all of these factors could provide the evidence necessary to determine whether a decrease in the volume and level of activity has occurred:

a. There are few recent transactions.

b. Price quotations are not based on current information.

c. Price quotations vary substantially either over time or among market makers (for example, some brokered markets).

d. Indexes 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, considering 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 or absence of a market for new issuances (that is, a primary market) for the asset or liability or similar assets or liabilities.

h. Little information is released publicly (for example, a principal-to-principal market).

7. If the reporting entity concludes that there has been a significant decrease in the volume and level of activity for the asset or liability in relation to normal market activity for the asset or liability (or similar assets or liabilities), transactions or quoted prices may not be determinative of fair value (for example, there may be increased instances of transactions that are a result of a forced or liquidation sale). Further analysis of the transactions or quoted prices is needed, and a significant adjustment to the transactions or quoted prices may be necessary to estimate fair value. Significant adjustments also may be necessary in other circumstances (for example, when a price for a similar asset requires significant adjustment to make it more comparable to the asset being measured or when the price is stale.)

8. If there has been a significant decrease in the volume and 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 weighing 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 estimates. The objective is to determine the point within that range that is most representative of fair value under current market conditions. A wide range of fair value estimates may be an indication that further analysis is needed.

9. Determining the price at which willing market participants would transact at the measurement date under current market conditions if there has been a significant decrease in the volume and level of activity for the asset or liability depends on the facts and circumstances and requires the use of significant judgment. However, a reporting entity's intention to hold or

12. In its determinations, a reporting entity need not undertake all possible efforts, but shall not ignore information that is available without undue cost and effort. A reporting entity would be expected to have sufficient information to conclude whether a transaction is part of a forced or liquidation sale when it is party to the transaction.

13. Regardless of the valuation techniques used, a reporting entity shall include appropriate risk adjustments. A fair value measurement should include a risk premium reflecting the amount market participants would demand because of the risk (uncertainty) 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 basis on which to exclude a “risk adjustment”. Risk premiums should be reflective of a transaction, other than a forced or liquidation sale, between market participants at the measurement date under current market conditions.

14. When estimating fair value, the fair value definition does not preclude the use of quoted prices provided by third parties, such as pricing services or brokers, when a reporting entity has determined that the quoted prices provided by those parties are determined pursuant to the fair value definition. However, when there has been a significant decrease in the volume or level of activity for the asset or liability, a reporting entity shall evaluate whether those quoted prices are based on current information that does not reflect forced or liquidation sales or a valuation technique that reflects market participant assumptions (including assumptions about risks). In weighing a quoted price as an input to a fair value measurement, a reporting entity should place less weight (when compared with other indications of fair value that are based on transactions) on quotes that do not reflect the result of transactions. Furthermore, the nature of the quote (for example, whether the quote is an indicative price or a binding offer) should be considered when weighing the available evidence, with more weight given to quotes based on binding offers.

15. This consensus has an effective date for interim and annual financial reporting periods ending on or after June 30, 2009. The effective date is restricted to prospective application and prohibits retrospective application to a prior interim or annual reporting period.

INT 09-04 Status

16. No further discussion planned.

