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The amendments would be effective for interim and annual reporting periods ending after December 15, 2009, except for the sensitivity disclosures about Level 3 measurements, which would be effective for interim and annual periods ending after March 15, 2010.

FASB Proposes Improving Disclosures About Fair Value Measurements.

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Background

On August 28, 2009, the FASB issued an exposure draft (ED) of a proposed Accounting Standards Update, *Improving Disclosures About Fair Value Measurements*. The ED is in response to recommendations by several constituents that the current fair value measurement disclosure requirements in ASC 820[1] (formerly Statement 157[2]) be improved. Comments on the ED are due by October 12, 2009.

The ED proposes new, and clarifies existing, disclosures about fair value measurements. Similar disclosures are already required by IFRS 7.[3] The amendments would be effective for interim and annual reporting periods ending after December 15, 2009, except for the sensitivity disclosures about Level 3 measurements, which would be effective for interim and annual periods ending after March 15, 2010.

This *Heads Up* summarizes the key disclosures proposed in the ED. The appendix of this Heads Up contains a brief overview of how the fair value disclosures in ASC 820 may change.

Disclosure Requirements

Level of Disaggregation

Some financial statement users noted that ASC 820's existing requirements to provide fair value measurement disclosures by "*major category* of assets and liabilities" are often interpreted to be a line item in the statement of financial position. They noted that disclosures at this high level of aggregation are less useful. The ED proposes that the disclosures now be provided for "each class of assets and liabilities." This requirement would often lead entities to provide disclosures at a more granular level than by line item in the statement of financial position. In determining the appropriate level of disaggregation, an entity would consider what is required for specific assets and liabilities under other U.S. GAAP (e.g., the disclosure level required for derivative instruments by ASC 815).[4]

The ED also proposes that in determining the appropriate classes of assets and liabilities, an entity should consider the nature and risks of the assets and liabilities as well as their placement in the fair value hierarchy (i.e., Level 1, 2, or 3). For example, a greater number of classes would be expected for fair value measurements using significant unobservable inputs (i.e., Level 3 measurements) because of the increased uncertainty and subjectivity involved in these measurements.

[1] FASB Accounting Standards Codification Topic 820, *Fair Value Measurements and Disclosures*.
[2] FASB Statement No. 157, *Fair Value Measurements*.
[3] IFRS 7, *Financial Instruments: Disclosures*.
[4] FASB Accounting Standards Codification Topic 815, *Derivatives and Hedging*.

The ED clarifies that disclosures about the valuation techniques and inputs used to measure fair value is required for both recurring and nonrecurring fair value measurements.

Sensitivity Analysis[5]

Financial statement users have indicated that information about the effect of reasonably possible alternative Level 3 inputs would be relevant to their analysis of the entity's performance. Thus, under the ED, for Level 3 fair value measurements, if changing one or more of the significant unobservable inputs to reasonably possible[6] alternative inputs would change the fair value significantly,[7] entities should state that fact and disclose the total effect of those changes. In addition, entities would need to describe how the effect of a change to a reasonably possible alternative input was calculated. The ED also proposes that an entity disclose, for each class of Level 3 measurements, quantitative information about the significant inputs used and reasonably possible alternative inputs. The sensitivity analysis disclosures would be required for both interim and annual periods.

Transfers Into and Out of Levels 1, 2, and 3

Under the ED, for assets and liabilities that are measured at fair value on a recurring basis in periods after initial recognition (e.g., trading securities) an entity would be required to disclose the amounts of significant transfers between Levels 1 and 2, and transfers into and out of Level 3, of the fair value hierarchy and the reasons for those transfers. An entity must disclose and discuss significant transfers **into** each level separately from transfers **out** of each level. Also, any significant transfers would be presumed to have occurred as of the beginning of the interim period in which the transfer occurred.

Reconciliation on a Gross Basis

The ED proposes to amend the reconciliation of the beginning and ending balances of Level 3 recurring fair value measurements. In periods after initial recognition, an entity would present information about purchases, sales, issuances, and settlements for significant unobservable inputs (Level 3) on a gross basis rather than as a net number as currently required. Financial statement users have indicated that gross presentation is more useful.

Disclosures About Inputs and Valuation Techniques

The ED clarifies that disclosures about the valuation techniques and inputs used to measure fair value is required for both recurring and nonrecurring fair value measurements. In addition, those disclosures are required for fair value measurements classified either as Level 2 or Level 3. If the valuation technique has changed, entities should disclose that change and the reason for the change.

[5] Sensitivity analysis would not be required for Level 3 fair value measurements related to the use of net asset value.

[6] *Reasonably possible* as used in this ED has the same meaning as in the Codification's glossary definition of contingencies (in the context of Topic 450). That is, it is defined as "the chance of the future event or events occurring is more than remote but less than likely."

[7] For this purpose, significance is judged with respect to earnings and total assets or total liabilities or, when changes in fair value are recognized in other comprehensive income, with respect to total equity.

Appendix

Recurring Fair Value Measurements

Topic	Existing Disclosures — Topic 820	ED's New or Amended Disclosures
Level of disaggregation	Provide disclosures by each "major category" of assets and liabilities	Provide disclosures by each "class" of assets and liabilities
Transfers into and out of Levels 1, 2, and 3	Transfers into and out of Level 3	Significant transfers between Levels 1 and 2 and the reasons for those transfers; the reasons for transfers into and out of Level 3
Level 3 reconciliation	• No separate disclosure of total gains and losses recognized in other comprehensive income • Purchases, sales, issuances, and settlements (net) • Transfers in and out of Level 3	• Total gains and losses recognized in other comprehensive income • Purchases, sales, issuances, and settlements (each type disclosed separately) • Transfers in and/or out of Level 3 (separately when significant) and the reasons for the transfers
Valuation techniques and inputs	The inputs and valuation technique(s) used to measure fair value and a discussion of changes in valuation techniques and related inputs, if any, during the period	For Levels 2 and 3, the valuation techniques and inputs used to determine fair values of each class of assets or liabilities; if the valuation technique has changed, disclose that change and the reason for the change
Sensitivity analysis	None	For Level 3, if changing one or more of the significant unobservable inputs to reasonably possible alternative inputs would change the fair value significantly: • State that fact. • Disclose the total effect of the change. • Describe how the effect of the change was calculated. • Disclose quantitative information about the significant inputs used and reasonably possible alternative inputs for each class of Level 3 fair value measurement.

Nonrecurring Fair Value Measurements

Topic	Existing Disclosures — Topic 820	ED's New or Amended Disclosures
Level of disaggregation	Provide disclosures by each "major category" of assets and liabilities	Provide disclosures by each "class" of assets and liabilities
Valuation techniques and inputs	The inputs and valuation technique(s) used to measure fair value and a discussion of changes in valuation techniques and related inputs, if any, during the period	For Levels 2 and 3, the valuation techniques and inputs used to determine fair values of each class of assets or liabilities. If the valuation technique has changed, disclose that change and the reason for the change.
Sensitivity analysis	None	For Level 3, if changing one or more of the significant unobservable inputs to reasonably possible alternative inputs would change the fair value significantly: • State that fact. • Disclose the total effect of the change. • Describe how the effect of the change was calculated. • Disclose quantitative information about the significant inputs used and reasonably possible alternative inputs for each class of Level 3 fair value measurement.

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