

MEMO# 25631

November 8, 2011

Draft Paper on Dollar Roll Transactions

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TO: ACCOUNTING/TREASURERS COMMITTEE No. 18-11 RE: DRAFT PAPER ON DOLLAR ROLL TRANSACTIONS

As you know, earlier this year the Financial Accounting Standards Board modified Topic 860, Transfers and Servicing. [\[1\]](#) The changes to Topic 860 eliminated the collateral maintenance provision that an entity may use to determine whether a transfer of securities in a repurchase agreement is accounted for as a sale and subsequent repurchase or a secured borrowing. The changes to Topic 860, which are effective for the first interim or annual period beginning on or after December 15, 2011, may cause certain dollar roll transactions that currently are accounted for as a sale and a subsequent repurchase to instead be characterized as a secured borrowing transaction. The Accounting Policy Subcommittee, with assistance from other industry participants, has prepared the attached draft paper intended to assist funds in applying the changes to Topic 860 to dollar roll transactions.

Topic 860

ASC Topic 860 prescribes when a transferor may recognize a sale upon the transfer of securities subject to repurchase agreements. That determination is based, in part, on whether the entity has maintained effective control over the transferred securities. If control is surrendered, the transferred security is removed from the transferor's balance sheet, and the transferor accounts for the cash received and an obligation to repurchase the security. When a transfer of securities does not qualify for sale accounting, it is accounted for as a secured borrowing. In a secured borrowing, the transferred security remains on the transferor's balance sheet and the transferor recognizes a liability for the cash received.

Sale accounting is achieved only if certain criteria are satisfied, including demonstrating that the transferor has surrendered effective control over the transferred security. The recent changes to Topic 860 remove one of the conditions necessary to conclude that a transferor has effective control by eliminating the requirement to hold cash or other collateral that is sufficient to fund substantially all of the cost of purchasing a replacement security, should the transferee fail to return the transferred asset. The recent changes make the amount of cash collateral received by the transferor irrelevant in determining

effective control.

Other criteria applicable to the assessment of effective control remain unchanged. The transferor would be deemed to have maintained effective control over the securities transferred (requiring secured borrowing accounting) for agreements that both entitle and obligate the transferor to repurchase the security if all of the following conditions are met:

1. The securities to be repurchased or redeemed are the same or substantially the same as those transferred;
2. The agreement is to repurchase or redeem them before maturity, at a fixed or determinable price; and
3. The agreement is entered into contemporaneously with, or in contemplation of the transfer.

Mortgage Dollar Rolls

A mortgage dollar roll is a transaction in which a fund sells a mortgage-backed security to a dealer and simultaneously agrees to repurchase a similar (but not the same) security in the future at a pre-determined price. Whether a mortgage dollar roll qualifies for sale accounting or instead is treated as a financing depends upon the particular facts and circumstances. For example, where the security to be repurchased is not the same or “substantially similar” then the transferor has not maintained effective control. The attached draft paper describes the applicable accounting literature, as well as considerations relevant to determining whether securities to be repurchased are substantially similar. For situations in which effective control is maintained and secured borrowing treatment is appropriate, the draft paper describes a methodology for calculating interest expense.

Please provide any comments you may have on the attached draft paper to the undersigned (202/326-5851 or smith@ici.org) or to Paul Roselli at Fidelity (603/791-6669 or paul.roselli@fmr.com) by November 23, 2011. We plan to discuss the attached, and any comments received, at the upcoming Accounting Treasurers Committee meeting on December 1.

Gregory M. Smith
Director - Operations/Compliance & Fund Accounting

[Attachment](#)

endnotes

[1] ASU No. 2011-03, Transfers and Servicing (Topic 860): Reconsideration of Effective Control for Repurchase Agreements. See Accounting/Treasurers [Memorandum No. 8-11](#) (May 2, 2011) [25160].