Students of Master of Professional Accountancy Program
Indiana University Kelley School of Business Indianapolis
801 W. Michigan Street
Indianapolis, IN 46202-5151

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Letter of Comment No: 23
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Ms. Suzanne Q. Bielstein
Director of Major Projects and Technical Activities
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5112
Norwalk, CT 06856-5116

Reference: Proposed Statement of Financial Accounting Standards, *Accounting for Servicing of Financial Assets an Amendment of FASB Statement No. 140*

Dear Ms. Bielstein:

On August 11, 2005, the Financial Accounting Standards Board ("FASB") issued the exposure draft for *Accounting for Servicing of Financial Assets an Amendment of FASB Statement No. 140.* The Board has requested commentary on this exposure draft. We appreciate the opportunity to offer our support and opinions to the ED. We are responding as a group of current and future accounting professionals in the Indiana University Master of Professional Accountancy Program at the Kelley School of Business Indianapolis.

We have observed the comments and suggestions from constituents within the financial investment industry and appreciate the steps taken by the Board to promote fair value reporting for servicing assets/liabilities without having to meet the effectiveness requirements required by FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities.* Within the constructs of the current ED, entities will have the opportunity to choose either fair value accounting or the amortization method with respect to separately recognized servicing assets/liabilities. We would like to see more principles-based guidance about how an entity should make that determination. We recommend that entities review the FASB Exposure Draft, *Fair Value Measurements,* for further guidance in determining whether to subsequently measure fair value for separately recognized servicing assets/liabilities. The fair value determinants in the fair value ED could provide a threshold for when to elect the amortization method in instances when a fair value determination can only be made with limited market data or indexes that would result in a more biased, internally-derived market value.

We support the Board's proposal to allow fair value measurement for servicing assets/liabilities, while maintaining the amortization method as an alternative when the assets/liabilities are not realistically indicative of a fair value determination. We believe fair value measurement will have a positive impact on comparability of financial reporting within the industry. The advantages of using the option for fair value measurement for servicing assets/liabilities will prove an effective incentive to drive the industry toward a more consistent valuation methodology. These advantages include simplification of accounting and disclosure requirements for hedging instruments that are currently quite complex under SFAS 133.

We believe the fair value measurement can increase reliability of financial reporting as it relates to the underlying economic substance of the transaction, when there is a readily obtainable and objective market for the instruments. In addition, fair value measurement offers the possibility of including on the income statement both the current market adjustments for servicing assets/liabilities and any related hedge to improve the current standards that often reflect artificial volatility in reported earnings that is not consistent with the underlying economic event. However, the major discrepancy that is imperative to address is the accounting standards for available-for-sale securities used as hedges as they currently exist under SFAS 115.

The Board has requested comments specifically related to transfer provisions allowing entities to transfer securities classified as available-for-sale to the trading category without calling into question an entity's treatment of such securities under FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. The reluctance to include such a provision came from the Board's concern over how to identify the securities for which this transaction would apply. We are concerned that these transition provisions will create an inconsistent motivation by entities that should be addressed in the interest of clear and consistent principles for quality financial reporting. For example, if an entity exercises the fair value option to measure separately recognized servicing assets/liabilities and the related financial instruments to offset the risks of those servicing assets/liabilities are classified as available-for-sale, gains and losses will not offset in the income statement. In this situation, an entity is encouraged to elect the amortization method in reporting separately recognized servicing assets/liabilities to minimize income statement volatility. Because the Board has specifically concluded that fair value is the most relevant attribute for initially recognizing all service rights, it seems that GAAP should reflect principles that encourage fair value reporting throughout the term of those service rights.

If the Board chooses to include transition provisions relating to reclassifying available-for-sale securities to the trading category, certain changes or amendments must be addressed. According to SFAS 115, "debt and equity securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities…" If an entity is allowed to transfer securities classified as available-for-sale to the trading category, more than likely it will not meet this "near term" criterion and most certainly not in all cases. The Board could address whether to add a separate subcomponent to the available-for-sale category which allows mark to market adjustments to be reflected in income or to provide certain criteria for which this type of transfer to the trading category is allowed.

We have determined that some specificity should apply with respect to the transition of securities among the categories defined in SFAS 115. First, transfers from any other category other than available-for-sale are outside the scope of this comment letter. Second, transfers from available-for-sale to any other category other than trading or some subcomponent of available-for-sale are outside the scope of this comment letter. Third, only the transfers of securities mitigating the risks of servicing assets/liabilities are within the scope of this comment letter. To summarize, we encourage the board to specifically address the principles underlying transfers of available-for-sale securities to the trading category to mitigate the risks inherent in separately recognized servicing assets/liabilities.

If a transition provision is included in the final standard, we also recommend that the transfer should be restricted to a one-time election to mirror the rules that apply to fair value accounting for servicing assets/liabilities. In other words, when an entity makes the irrevocable election to apply fair value accounting for a class of existing or new servicing assets/liabilities, the transfer of the available-for-sale derivatives that mitigate the risks of those related servicing rights should be applied simultaneously and irrevocably. In addition, additional disclosure requirements for these one-time transfers will be necessary.

We recognize that convergence with international accounting standards is embodied within the language of more recent authoritative accounting literature. With respect to the current ED, there are some international developments which coincide with the recommended transfer provisions. Specifically, IASB's Press Release in June 2005 amending the fair value option in IAS 39, *Financial Instruments: Recognition and Measurement*, allows entities to irrevocably designate financial assets/liabilities that meet certain criteria to be measured at fair value through current income. This amendment is effective January 1, 2006, with early application encouraged. Even though the current amendment is more restrictive than the 2003 revisions of IAS 39, available-for-sale securities used to mitigate risks for servicing assets/liabilities are eligible to be measured at fair value through current income. We encourage the Board to consider this provision in determining how to address the transition of available-for-sale securities used to hedge separately recognized servicing assets/liabilities.

In conclusion, we are in favor of the Board's direction toward fair value measurement for servicing assets/liabilities. However, we respectfully request the inclusion of the transfer provisions and the suggested restrictions with the conviction that this will produce clearer and more consistent accounting principles. We commend the Board's convergence efforts with international accounting standards and conclude that the transfer provisions will serve to move us closer to the goal of convergence by more similarly reflecting the provisions allowed under the amended IAS 39.

Respectfully submitted,

Jason Arnett

Brian Hanson

Jill Lambert

Jingmei Xu