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LETTER OF COMMENT NO. 2

Ladies/Gentlemen:

I am writing you today to discuss the recent rescission of Implementation Issue D1 with respect to FAS 133, Accounting for Derivative Instruments and Hedging Activities with FAS 155, Accounting for Certain Hybrid Financial Instruments. I have some genuine concerns over the implementation of FAS 155 as it relates to Mortgage Backed Securities (MBS) and the implications for my institution, some confusion on the necessity of implementation given FAS 91 and a need for some clarification.

First, I would like to address some of my concerns regarding FAS 155 with respect to MBS as they relate to my institution. The bank that I work for, Fiserv Trust Company, utilizes MBS as its primary source of income funded by our deposits. As a "Special Purpose Bank" our State charter as a deposit taking Trust Company will not allow us to make loans. We utilize MBS as a primary source of income in the same manner that a traditional bank would use loans that they've underwritten. Just because our loans are securitized and another institution's are not should not warrant different accounting treatment. This will create a loss of parity between my institution and other banks. In one of the examples in FAS 133, paragraphs 224-228, the example focuses entirely on the changes in the swap value while ignoring the changes in the loan values. Had these loans been securitized the changes in market values would be required by FAS 155. I guess I don't see a difference in the Interest Rate Risk (IRR) of a loan that has or hasn't been securitized.

By implementing FAS 155 my ability to manage the banks IRR through Asset Liability Management (ALM) practices has been reduced. This I'm sure is an unintended consequence of the Statement which punishes bonds purchased at a discount and thus favors bonds purchased at par or a premium. I'm not sure why this Statement would only focus on the doubling of returns while ignoring returns being halved or negative returns. In managing my institution's IRR through ALM there are many instances where a discount security would help me balance my institution's IRR. This Statement impairs my ability to practice ALM by making it impractical to purchase securities at a discount which could help me manage my portfolio's net premium or discount. FAS 155 completely ignores modern portfolio theory and instead focuses on single security designations. In order to shorten or lengthen my portfolio's duration and therefore market risk, I need the full spectrum of investments (CMOS & Pass-Throughs) at my disposal. By singling out an asset class (CMOS due to their structuring) my tools to manage IRR are severely hampered versus another institution who can easily favor the underwriting of long or short term loans.

I believe FAS 115 and its original logic in treating investments with respect to holding periods to be an inherently logical proposition. All mainstream fixed income investments will revert to par at maturity but different holding horizons should have different accounting treatment as the risk to the institution depends on the holding period. FAS 115 understands this and accounts for this beautifully. By forcing short term volatility in earnings on an institution, through market to market accounting (Trading designation), who intends to hold a security to maturity has an unintended consequence of altering future business plans to account for this unwarranted volatility in earnings. In other words, it forces my company to take short term considerations into account when making long term decisions. The Available for Sale designation is also inappropriate for my institution as the same information can be derived by investors by combining the Equity and Unrealized Gain/Loss components of the Balance Sheet. The Hold To Maturity option is the only viable option for my institution and with the FAS 91 Retrospective Methodology we employ, any changes in market conditions are reflected in earnings.

FAS 91 Retrospective Methodology already requires that changes in market conditions be reflected in financial statements. With periodic changes to MBS prepayment assumptions to reflect current market conditions, the implementation of FAS 91 adequately forces changes to Book Value on the Balance Sheet and through this mechanism conveys these changes to the Income Statement as well. While not a true mark to market mechanism it is a reasonable substitute given the intent to Hold To Maturity. This methodology considers historical cash flows as well as projected cash flows in an effort to maintain a level yield on the security. Changes in assumed future prepayment behavior are applied to both historical and prospective cash flows to maintain this level yield. The adjustment for past amortization/accretion "errors" in light of current market conditions are transmitted to both the Balance Sheet and Income statement quite efficiently. Unlike FAS 155 which requires fair valuation by taking changes in market value into current income, FAS 91 does not violate the matching principle in accounting. A change in market value implies a change in the value of an income stream that may occur over several reporting periods or years. FAS 91 only adjusts, in the current period, for "errors" made in amortization and accretion in prior periods. The FAS 91 methodology, without prejudice, forces securities to par at maturity regardless of whether they were purchased at a premium or discount.

Lastly, some points needing clarification. In FAS 155, Amendments to Statement 133, 4b:

1. (by reference paragraph 13a in FAS 133) what would be considered "substantially all" of the initial recorded investment?
2. (by reference paragraph 13b in FAS 133) under what prepayment assumptions would this apply? A completely unrealistic prepayment assumption of a security prepaying within a few months of issuance? A reasonable Broker/Dealer estimate of an unlikely or probable prepayment assumption? For example, at purchase, the -300 or 0 Bloomberg Median Prepayment Speed?

Ladies/Gentlemen, I realize my concerns are tardy with respect to the implementation of FAS 155 but I believe it's important that you understand the wide ranging effect of this pronouncement on my institution and many others. Without this dialogue it would be impossible for you to do your jobs effectively. I anxiously await a response and hope you reconsider re-instating FAS 133 Implementation Issue D1 or address my concerns in some other measure that will eliminate the problems created for my institution by this Statement.

Sincerely,

Todd J. Stuka, CFA
Director, Portfolio Management
Fiserv Trust Company
303 824-6342