



December 8, 2006

LETTER OF COMMENT NO. 14

Mr. Lawrence W. Smith
Director, Technical Application and Implementation Activities and EITF Chair
Financial Accounting Standards Board
401 Merritt 7
P. O. Box 5116
Norwalk, CT 06856-5116

File Reference: Proposed Issue B40

Re: Proposed Statement 133 Implementation Issue No. B40, "Embedded Derivatives: Application of Paragraph 13(b) to Securitized Interests in Prepayable Financial Assets"

Deloitte & Touche LLP is pleased to comment on proposed Statement 133 Implementation Issue No. B40, "Embedded Derivatives: Application of Paragraph 13(b) to Securitized Interests in Prepayable Financial Assets." Although we support the issuance of the proposed Implementation Issue, we recommend deletion of condition (b).

To meet condition (b), the underlying financial assets cannot contain an embedded derivative that requires bifurcation. However, the conditions do not preclude, as an underlying position in a securitization, a freestanding derivative. It seems inconsistent that freestanding and embedded derivatives would not be given equivalent treatment because both can identically affect cash flows regardless of the contractual form (i.e., the presence or absence of a host) the derivative takes.

To resolve the inconsistency, the staff should delete condition (b). Whether an embedded derivative exists under paragraph 13(b), in the context of prepayable securitized financial assets, should principally depend on whether there is an embedded derivative in the beneficial interest (condition (c)) whose benefit can be obtained by the investor (condition (a)).

This recommendation is consistent with the approach of FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments*, as articulated in paragraph 4(b). Analyzing whether a securitized financial interest embeds a derivative starts with understanding the contractual terms of the beneficial interest itself. A *substantive* understanding of the contractual terms involves understanding the securitized instruments because their interplay generates the deal's cash flows. As the example in paragraph 200B indicates, the presence of a stand-alone derivative does not necessarily mean that the beneficial interests have an embedded derivative.

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If the staff does not delete condition (b), an explanation of why it is needed would be helpful.

Deloitte & Touche LLP appreciates the opportunity to comment on the proposed Implementation Issue. For questions about our comments, please contact Georganne Walters at (203) 761-3102.

Yours truly,

Deloitte & Touche LLP

cc: James Johnson