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October 30, 2008

Mr. Russell G. Golden
Technical Director
Financial Accounting Standards Board
401 Merritt 7
P. O. Box 5116
Norwalk, CT 06856-5116

File Reference No.: 1610-100
Re: Proposed FASB Statement, *Accounting for Transfers of Financial Assets* — an amendment of FASB Statement No. 140

Dear Mr. Golden:

Deloitte & Touche LLP is pleased to comment on the FASB's proposed Statement, *Accounting for Transfers of Financial Assets* — an amendment of FASB Statement No. 140 (the "proposed Statement").

We support the Board's efforts to improve financial reporting by enterprises involved with transfers of financial assets and to increase the relevance and transparency of the related disclosures. However, we do not support the issuance of the proposed Statement as currently drafted because it represents a significant change to the existing derecognition model that will most likely require significant and costly changes to accounting systems and controls that will most likely only be effective for a short time.

Rather than issuing this proposed Statement as a final standard, the FASB should work with the IASB to develop a common derecognition model that can be applied by all entities reporting under either U.S. GAAP or IFRSs. Currently, the two boards are expected to issue joint final standards by 2010. Therefore, if the FASB were to issue this proposed Statement as a final standard, U.S. registrants would have to apply three different derecognition models within a short time frame, resulting in operational challenges for preparers.

Because derecognition and consolidation are inextricably linked, we also strongly encourage the FASB and IASB to concurrently develop a common consolidation principle. The derecognition and consolidation principles should be conceptually consistent, based on the concept of control, and consistent with the definitions of an asset and a liability being developed in the joint conceptual framework. We believe that such consistent principles are fundamental to more faithfully representing the assets and liabilities of a reporting entity.

A jointly developed derecognition model and principles that receive full due process will also highlight unintended consequences. For example, we do not believe that the Board has sufficiently weighed the effects of eliminating the concept of a sale of a portion of a financial asset. In a transaction in which the underlying economics are both the sale of a portion of a financial asset and a financing transaction, the entire transaction would be accounted for as a secured borrowing under the proposed Statement and the related amendments to the FASB Staff Implementation Guide (Statement 140).[1] This could be achieved by the transfer of the financial asset and the retention of a call option when the transferred principal balances have been reduced to a predetermined amount for the portion that represents a financing transaction. We are concerned that the proposed accounting treatment may not mirror the underlying economics of the transaction. The FASB and IASB, with the assistance of preparers and users of financial statements, should carefully analyze the impact of the new derecognition model as the joint standard is developed.

We acknowledge that if the FASB were to remove the project from its agenda and develop a joint standard with the IASB, the recent practice issues would not be addressed until such standard becomes effective. We therefore support requiring increased disclosures in the interim. (See our October 15, 2008, comment letter to the Board regarding proposed FSP FAS 140-e and FIN 46(R)-e[2] (the "proposed FSP").)

If the Board determines that it must issue the proposed Statement, it should consider revising it in accordance with our comments and suggestions below.

Effective Control — Transferee Constraint (Paragraph 9(c)(3))

The concept that a "constraint is **designed primarily** to provide the transferee with a benefit" (emphasis added) in paragraph 9(c)(3) of the proposed Statement is not operational. Specifically, we believe that it will be difficult for a transferor to conclude that the transferee has **primarily benefited** from a constraint on its ability to pledge or exchange transferred financial assets that it has received. For example, this concept is difficult to reconcile when the restriction on a transferee that is a special-purpose entity (SPE) is established by the transferor as contemplated in paragraph 54A of the proposed Statement. Although the Board concluded that the constraint of the transferee was designed primarily to benefit the transferee in marketing securities to potential beneficial interest holders, we believe that it is often the transferor that benefits from the ability of the SPE to market securities backed by the transferred financial assets to beneficial interest holders. This benefit is evidenced by the transferor obtaining proceeds associated with a securitization transaction at a lower cost than those in an unsecured debt issuance. The transferor is usually involved in the design of the securitization vehicle and will typically structure the transaction to meet its needs and those of the guarantor, if any. It is unlikely that the transferor will design restrictions on the transferability of the transferred financial assets primarily for the benefit of the transferee. In addition, when the transferor obtains a beneficial interest (e.g., through a guarantee, a residual interest in the transferred assets, or a servicing arrangement), it may not be possible to determine whether it is the transferor or the transferee that is receiving the primary benefit of the constraint.

The Board should allow the transferor to look through an SPE and determine whether the beneficial interest holders have any restrictions on their ability to pledge or exchange their investments in an SPE. The Board would need to ensure that it clearly defines an SPE to prevent implementation issues similar to those experienced by entities accounting for qualifying SPEs.

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[1] FASB Staff Implementation Guide (Statement 140), "A Guide to Implementation of Statement 140 on Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities."
[2] Proposed FASB Staff Position No. FAS 140-e and FIN 46(R)-e, "Disclosures About Transfers of Financial Assets and Interests in Variable Interest Entities."

Effective Control — Ability to Reacquire Transferred Assets (Paragraph 9(c)(2))

Paragraph 9(c)(2) should be clarified to acknowledge the exceptions (in addition to cleanup calls) in paragraphs 52 and 54 that sale accounting is not precluded if the transferor has either (1) the unilateral ability to reacquire the transferred assets but the reacquisition price is so deep out of the money as of the transfer date that it is probable that the right will not be exercised or (2) a freestanding call option written by the transferee for transferred financial assets that are readily obtainable in the marketplace. Currently the only exception in paragraph 9(c)(2) is that related to cleanup calls.

Effective Control — Transferee Constraint (Paragraph 9(c)(1))

The requirements in paragraph 47(d) should be consistent with those in proposed paragraph 8A. The Board should therefore consider the following wording changes to paragraph 47(d) (added text is underlined and deleted text is ~~struck out~~):

> "d. The agreement is entered into ~~concurrently~~ contemporaneously with or in contemplation of the transfer."

Legal Isolation (Paragraph 9(a))

We believe that the following amendments will provide further clarification on the legal isolation criteria.

Proposed paragraph 27A clarifies that legal opinions often are necessary to support a conclusion that a transfer of financial assets are isolated from the transferor. The descriptions of a true sale opinion and a nonconsolidation opinion in proposed paragraphs 27A(a) and 27A(b) are based on the auditing guidance in AU Section 9336.[3] We support including these descriptions in the proposed Statement and believe they provide useful information to financial statements preparers. However, we suggest that the remaining provisions (including the guidance applicable to banks subject to FDIC receivership) from AU Section 9336 also be included in the final Statement. This would clarify that it is management's primary responsibility, not that of auditors, to support any assertions that transferred financial assets are legally isolated. We believe that guidance in the final Statement on what constitutes an acceptable legal opinion is equally relevant to financial statement preparers. We also believe that the Board should consider including some of the information in the Background Information and Basis for Conclusions section, such as the discussion on set-off rights in paragraph A14, in the standard section of the final Statement, because otherwise it will be omitted from the codified accounting standards.

We also suggest that the Board clarify whether a transfer of financial assets from one subsidiary to another subsidiary with a common parent can achieve legal isolation in the stand-alone financial statements of each subsidiary irrespective of whether legal isolation could be achieved in the common parent's consolidated financial statements. That is, we believe that it is unclear whether a different isolation conclusion can be reached in a subsidiary's stand-alone financial statements when it was determined that the legal isolation requirement was not achieved in the parent's consolidated financial statements. We suggest that the Board include its response to question 20 of the FASB Staff Implementation Guide (Statement 140) as amended by paragraph 27A of the proposed Statement.

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[3] AICPA and PCAOB *Professional Standards*, AU Section 9336, "Using the Work of a Specialist: Auditing Interpretations of Section 336."

We also suggest that the final Statement include the concepts in the implementation guidance in the responses to questions 19–19D of the FASB Staff Implementation Guide (Statement 140) regarding whether transferred assets can be isolated from a transferor that is subject to receivership by the FDIC. This will ensure that the guidance is appropriately considered and applied consistently across all applicable entities.

Transfers to Consolidated Affiliates

It appears that paragraph 9 as revised by the proposed Statement requires that the transferor first apply the guidance in ARB 51[4] and Interpretation 46(R)[5] to determine whether the transferee will be consolidated before determining whether the transfer of financial assets should be accounted for as a sale. However, a transferor may transfer assets to a transferee in which it holds no other interests, and as part of the transaction the transferor may receive a controlling financial interest in the transferee (e.g., the power to direct activities through a servicing arrangement and significant benefits through a beneficial interest) and accordingly now be required to consolidate the transferee. It is unclear whether paragraph 9 would require the original sale to be unwound as the consolidated affiliate would maintain effective control of the financial assets. The Board should clarify in which order a transferor should apply the consolidation principles and derecognition principles and the effect of this order.

Participating Interests (Paragraph 8B)

The Board should clarify that the requirements in proposed paragraph 8B(b) stating, "**All** cash flows received from the assets are divided among the participating interests . . . in proportion to the share of ownership represented by each" (emphasis added) relate only to cash flows received from the date the participating interests are sold by the transferor. As proposed, the requirement that the "transferor's ownership shares must remain pro rata over the **life of the original asset**" (emphasis added) could be interpreted to require that all cash flows over the life of the original asset need to be divided proportionately, even when the participating interest was sold after the origination date of the financial asset. In addition, this would allow the originating lender in a bank participation loan to exclude origination fees (e.g., documentation fees, title fees) that are received before the sale of the participating interest when the originating lender identifies the cash flows that are divided among the participating interests. The language in the proposed Statement appears to indicate that these fees would not be excluded from the allocated cash flows, which would result in most participating loan agreements (when the originator receives originating fees before the sale of the participating interests) to fail sale accounting.

In addition, it is unclear whether the requirement to allocate all cash flows received from an asset to each participating interest excludes the cash flows received that represent the transferor's gain or loss on the sale of a portion of a financial asset. Because a participating interest in an asset may be sold after the purchase or origination of the asset, often the interest rate passed through for the portion of the asset sold is based on the market rate at the time of sale and differs from the contractual coupon on the financial asset. Generally, this difference is attributable to changes in market interest rates between the origination of the financial asset and the sale of the participating interest. For example, if an entity originates a loan with a contractual coupon of 8 percent but subsequently sells a portion of that loan, in a declining interest rate environment, for a 6 percent coupon, the retained 2 percent coupon is effectively the transferor's gain on sale of the portion of the loan sold. However, because cash flows

[4] Accounting Research Bulletin No. 51, *Consolidated Financial Statements.*
[5] FASB Interpretation No. 46(R), *Consolidation of Variable Interest Entities* — an interpretation of ARB No. 51.

equal to 8 percent are received on the portion of the loan sold, it is unclear whether an allocation of cash flows equal to only a 6 percent coupon to participating interests would meet the requirement in paragraph 8B(b). Under the proposed Statement, the transferor would need to (1) sell the participating interest at either a discount or a premium or (2) build (reduce) the excess interest into (from) the servicing fee. However, the issuance of participating interests at discounts or premiums will introduce significant prepayment risks associated with these investments, which may make them less attractive to market participants. We suggest that the Board clarify whether sale accounting is permitted if the transferor in a participation transaction retains an interest-only strip equal to the gain in the transfer.

Elimination of the Qualifying SPE Concept

Although the implementation issues related to whether an SPE is considered a qualifying SPE are eliminated by the proposed Statement, financial statement preparers will need to address new issues as part of the consolidation evaluation under the proposed amendments to Interpretation 46(R). For example, the subjective criteria for determining whether an SPE is a qualifying SPE will be removed and replaced by equally subjective criteria for determining who "has the power to direct matters that most impact the activities of the entity." For entities whose activities are prescribed by a trust agreement and servicing guide, it may be difficult to determine who "has the power to direct matters that most impact the activities of the entity." We agree with the Board's decision to eliminate the concept of a qualifying SPE provided that there are significant improvements made to the proposed modifications to Interpretation 46(R). These are discussed more fully in our separate comment letter on the proposed amendments to Interpretation 46(R).

Elimination of the GMS Exception

The proposed Statement seeks the elimination of the GMS (guaranteed mortgage securitizations) exception in Statement 140 by requiring that an enterprise only reclassify loans to debt securities if the transfer of the loans meets the requirements for sale accounting under paragraph 9 of Statement 140. The amendments will also eliminate the requirement in paragraph 9 of Statement 140 that the transferor can only recognize transferred financial assets as a sale to the extent that consideration other than a beneficial interest is received in the exchange. If the securitization meets the definition of a sale, these amendments will allow a transferor to reclassify loans-held-for-sale to investment securities when the transferor receives all of the investment securities in a GMS.

However, the additional requirement in paragraph 9(c)(3) makes it unclear whether the transfer will result in a typical GMS transaction qualifying for sale accounting because the transferor will benefit from the restriction placed on the transferred assets when it markets the investment securities. If the transferor takes back all of the beneficial interests, it is unclear whether it would need to record the debt securities and a liability to the trust for all of the beneficial interests on the basis of the amendments to paragraph 12 of the proposed Statement. If so, the trust, which, on the basis of Example 5 in the proposed amendments to Interpretation 46(R), would be consolidated by the guarantor, would record a receivable from the transferor equal to the transferor's liability. If the transferor subsequently sells the beneficial interests, the trust would need to reclassify the receivable from the transferor to mortgage loans. We do not believe that it is feasible for the nontransferor entity that must consolidate the trust to prepare its financial statements based on actions, taken by the transferor, that it may not be aware of.

Disclosure Requirements

The amendments proposed by the Board will result in the elimination of the example disclosures in Statement 140. We believe that on the basis of the number of additional disclosures proposed, the Board should consider expanding the examples that are already in Statement 140 rather than eliminating the example disclosures. This would assist with financial statement preparation.

Our October 15, 2008, letter to the FASB commented on the disclosure requirements in the proposed FSP. The disclosure requirements in the proposed Statement are similar to those required by the proposed FSP. We therefore recommend that the Board review our comments on the disclosure FSP. However, we would like to reiterate our concerns related to the requirement that companies disclose implicit arrangements related to a transfer. Specifically, we are concerned about the auditor's ability to obtain a reasonable level of assurance that the disclosures related to implicit arrangements in a transfer, as required in paragraph 17(i)(1) of the proposed Statement, are complete and accurate. Implicit arrangements are generally based on management's intention and are tied to the occurrence or nonoccurrence of a contingent future event that is outside the enterprise's control.

We would also like to draw the Board's attention to the fact that the proposed Statement does not include the disclosure requirements in paragraph 17(i)(1) of the proposed FSP that are related to the details of the SPE receiving the transferred assets.

Miscellaneous item

We suggest that the Board consider the following wording changes to paragraph 12 (added text is underlined):

> The transferor shall continue to report the transferred financial assets in its statement of financial position with no change in their measurement basis.

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Deloitte & Touche LLP appreciates the opportunity to comment on the proposed Statement. Please direct questions or comments to John Sarno at (203) 761-3433 or Trevor Farber at (203) 563-2547.

Yours truly,

Deloitte & Touche LLP

cc: Robert Uhl
Martin Rosenblatt