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Via email

LETTER OF COMMENT NO. 19

Russ Golden - Technical Director
Financial Accounting Standards Board
File Reference No. 1025-300
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: Invitation to Comment – FASB Staff Proposal EITF 99-20-a,
*Amendments to the Impairment and Interest Income Measurement
Guidance of EITF Issue No. 99-20*

Wells Fargo & Company (Wells Fargo) is a diversified financial services company which provides banking, insurance, investments, mortgages and consumer finance services. We appreciate the opportunity to comment on the issues being considered by the Board to achieve a more consistent determination of whether other-than-temporary impairments (OTTI) of debt securities have occurred and we strongly agree with the Board's rationale to amend EITF Issue No. 99-20, *Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests That Continue to Be Held by a Transferor in Securitized Financial Assets* (EITF 99-20) to require that debt securities subject to EITF 99-20 be evaluated for OTTI in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities* (FAS 115). The amendment will result in a single model for determining OTTI recognition for debt securities under U.S. GAAP. The proposed amendment is a required "fix" to eliminate inconsistent and misleading accounting outcomes for securities with similar credit facts and circumstances. The differing OTTI accounting determinations under these standards have been highlighted by current market conditions. We believe that failure by the Board to immediately adopt its proposed amendments to EITF 99-20 will result in material overstatements of OTTI on securitized asset investments where there has not been any material change in underlying credit or cash flows.

We regard the proposed amendments as an important initial step to improve financial reporting for OTTI. Application of current accounting standards results in different OTTI outcomes for similar securities with similar risks, caused by having two different OTTI accounting models. The primary inconsistency in the determination of OTTI between the two models is the evaluation of a security's credit risk – that is, the risk of not collecting future cash flows according to the security's contractual terms. We can think of no justification for evaluating credit risk differently based upon the form of a security when the substance is the same.

Investments in securitized assets rated below 'AA' at initial acquisition are subject to the EITF 99-20 model. However, investments in securitized assets rated 'AA' or above at initial acquisition or investments in non-securitized assets such as corporate/municipal bonds are subject to the FAS 115 model. The result is debt securities that have similar credit quality are evaluated for OTTI differently. Additionally, because the scope assessment of EITF 99-20 is required only when the security is initially recognized by the acquiring reporting entity, rating changes (e.g., downgrades) can result in application of two different OTTI models for the *same security*, depending solely upon when the security was initially acquired by a reporting entity. We don't understand how such arbitrary accounting promotes comparability nor do we believe that the required use of "market participant" cash flows to determine OTTI to be a sound determinant, especially given the current market environment. In the current market, there are often very limited or nonexistent market participants. In fact, the determination of OTTI on EITF 99-20 securities is primarily being based on indicative broker quotes due to the lack of any meaningful levels of actual trades, which has created an arbitrary OTTI process replete with "bright lines" and "rules of thumb". The existing EITF 99-20 approach to OTTI is completely at odds with the use of management credit and cash flow analysis which has created a fundamental disconnect between GAAP and management's required Sarbanes-Oxley certification. Therefore, we applaud the Board for moving to a single OTTI recognition model for debt securities and securitized assets.

Our comments regarding the Board's specific questions are as follows:

- 1. Issue 99-20 applies to beneficial interest that are not of a high credit quality or that can be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment. Other debt securities (for example, a corporate bond) with similar credit quality are not within the scope of Issue 99-20. The Board decided that similar instruments should be subject to the same impairment model. Do you agree with the Board's decision? Does the presence of prepayment risk warrant a different impairment model?*

Response:

We agree with the Board's decision that there should be a single impairment model for debt securities based on FAS 115 and that the existence of prepayment risk should not dictate a more sensitive accounting trigger for the recognition of impairment. Currently, a debt security within the scope of EITF 99-20 requires OTTI recognition if the reporting entity's estimate of cash flows that a market participant would use in determining the fair value of the security has adversely changed. Accordingly, use of market participant assumptions in developing cash flow estimates is required and cannot be overcome by reasonable management judgment regarding the probability of collecting future cash flows, regardless of whether or not the underlying assets are performing. For most EITF 99-20 debt securities, existing infrastructure in the financial markets does not provide reporting entities with readily available market participant cash flows. Therefore, in practice, determination of whether these cash flows have deteriorated is determined

based upon what the security's fair value (or market yield imputed using fair value) implies about a market participant's view of the cash flows. A decline in fair value (or increases in market yield) to a certain level is considered prima facie evidence by independent auditors of an adverse change in estimated cash flows that market participants are signaling, which triggers OTTI recognition regardless of the probability of collecting the cash flows. In dislocated markets, EITF 99-20 securities can experience severe price declines due to factors other than credit risk (e.g., liquidity risk). This scenario has been exemplified by securities having experienced price declines while either the underlying assets are fully performing or significant protection against credit losses exists. We believe recognition of OTTI in such instances, because credit risk is *presumed* to have deteriorated *solely* based upon fair value declines (or market yield increases), is not appropriate and is not what EITF 99-20 intended. Our response to this presumption is that the current low price / high yield required in the market is not a reflection of high expected losses in the investment security, but rather a by-product of the massive liquidity premium that is required in the market under current conditions for EITF 99-20 securities. This liquidity premium can be observed in the low prices / high yields required for even very senior AAA-rated investments of which few market participants would accuse of having any reasonable risk of credit loss. To illustrate our point, we have provided examples in **Appendix A** of EITF 99-20 securities that trade at low enough dollar prices (and consequently high enough market yields) to automatically require recognition of OTTI by independent auditors; however, the investments have few, if any, credit issues. EITF 99-20 was drafted when securitization transactions were less complex, markets were functioning normally and the "screen price" of transactions actually reflected a security's credit risk. However, practice and market conditions have evolved such that the model is no longer workable. Accordingly, we believe and agree with the Board that EITF 99-20 is not the appropriate go-forward model for OTTI recognition.

As long as an entity has the intent and ability to hold investments in debt securities to recovery of the unrealized loss (which may be maturity), we believe the fundamental determinant for OTTI recognition should be credit risk, that is, the risk that principal and interest payments will be collected according to the security's contractual terms. We believe a security's credit risk requires OTTI to the extent it becomes probable that cash flows will not be collected as contractually scheduled. Evaluation of credit risk for debt securities that are securitized financial assets requires evaluation of the credit quality of the underlying assets, how the cash flows from the underlying assets are distributed to the beneficial interest holders (cash flow waterfalls) and the subordination or other credit protection that exists relative to the reporting entity's beneficial interest that will absorb credit losses on the underlying asset pool. Assessing the probability of collecting future cash flows for EITF 99-20 securities requires careful study of these elements and application of reasonable management judgment, particularly in dislocated markets. FAS 115 requires the recognition of OTTI if it is probable the investor will be unable to collect contractually scheduled principal and interest payments. FAS 115 does not require exclusive reliance on a market participant's view of expected cash flows, thereby allowing for reasonable management judgment for assessing probability of collecting future cash flows. Accordingly, we support elimination of the EITF 99-20 OTTI model and use of the guidance provided in

paragraph 16 of FAS 115 for determining whether a debt security's credit risk requires OTTI recognition.

2. *The FSP amends Issue 99-20 to align the Issue 99-20 impairment model with the Statement 115 impairment model, resulting in a consistent determination of whether other-than-temporary impairment of available-for-sale or held-to-maturity debt securities have occurred. Statement 115 requires entities to assess whether it is probable that the holder will be unable to collect all amounts due according to the contractual terms. Is the Statement 115 impairment model operational for beneficial interest that were previously within the scope of Issue 99-20*

Response:

We believe the Statement 115 impairment model is operational for securities currently within the scope of Issue 99-20 as their contractual cash flows are readily determinable. The use of the FAS 115 model actually reduces the complexity of financial reporting by utilizing an impairment model for debt securities that is similar to existing models utilized for evaluating impairment for investments in loans under FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loans, an amendment of FASB Statements No. 5 and 15* (FAS 114). Under both FAS 115 and FAS 114, an impairment charge is recognized in earnings if it is probable the investor/creditor will be unable to collect cash flows as contractually scheduled. Furthermore, we believe it is appropriate to evaluate impairment for investments in loans and investments in beneficial interests in securitized assets (where loans are often the underlying assets) similarly and that the impairment evaluation should focus on the presence of credit risk, and not other risks (e.g., market risk or liquidity risk), in the instruments. Additionally, we encourage the Board to amend the FAS 115 model for OTTI measurement to be more consistent with FAS 114 impairment measurement for loans. We believe that since credit risk is the primary trigger for OTTI recognition when management has both the intent and ability to hold a security to recovery (or maturity), the measurement of any impairment charge should be based upon the credit risk component of the loss. Measuring OTTI equal to the difference between cost and fair value of the security results in impairment charges recognized in earnings unrelated to the risk(s) that triggered OTTI recognition (e.g., liquidity risk, interest rate risk and other market risks). Use of FAS 114 loan impairment model would more appropriately align OTTI measurement with OTTI recognition model.

3. *The Board is proposing that the FSP be effective for interim (including the fourth quarter for an SEC registrant) and annual reporting periods ending after December 15, 2008, applied prospectively. Do you agree with the proposed effective date? Should the Board consider making the FSP effective for periods beginning after December 15, 2008?*

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Response:

We agree with the proposed effective date.

Conclusion

In summary, we agree with the Board's proposed amendment to utilize the FAS 115 model for assessing OTTI for investments in all debt securities. We believe the FAS 115 model is an appropriate and operational model for assessing OTTI for securities within the scope of EITF 99-20. The proposed amendment represents a significant improvement to financial reporting, we agree with the Board that the FSP should be effective immediately (4th quarter for calendar-year companies) and not delayed until 2009. In addition, we encourage the Board to continue its work with the IASB on reviewing the overall FAS 115 OTTI measurement model. We believe that since credit risk is the primary trigger for OTTI recognition when management has both the intent and ability to hold a security to recovery (or maturity), the measurement of any impairment charge should be based exclusively upon the credit risk component of the loss.

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We appreciate the opportunity to comment on the issues contained in the Board's invitation. If you have any questions, please contact me at (415) 222-3119.

Sincerely,

/s/ Richard D. Levy

Richard D. Levy
Executive Vice President & Controller

CC: Ms. Donna Fisher, American Bankers Association
Ms. Gail Haas, New York Clearinghouse Corporation

Appendix A

In the table below are current price and yield ranges for two asset classes of structured securities that have experienced few defaults to date – commercial mortgage-backed securities (CMBS) and collateralized loan obligations (CLOs, where the underlying assets are senior bank loans). As can be seen, prices are very depressed and yields are very high, resulting in many securities breaching the thresholds set by some independent auditors for impairment under EITF 99-20. For context, given current LIBOR levels, market yields for floating rate forms of these securities, were they to be valued at par, as they were at new issue, would range from 2.50% to 3.75%.

Asset Type	Rating	Price Range* at 11/28/08	Yield Range at 11/28/08
Commercial Mortgage-Backed Securities (CMBS)	Senior AAA	52-65	14% area
	Junior AAA	25-30	30% area
	AA	15-20	45% area
	A	12-17	50% area
	BBB	10-15	>50%
Collateralized Loan Obligation (CLO)	AAA	75-80	8-10%
	AA	35-40	10-15%
	A	25-30	20-30%
	BBB	15-20	25-40%

* Prices are stated relative to a value of 100 (cents on the dollar) at new issue.

Below we cite four examples of structured securities that trade at very low dollar prices (i.e., high yields) and, thus, may be considered impaired under EITF 99-20, but which have few, if any, credit issues.

Example 1. Bear Stearns Commercial Mortgage 2006-T24 Class AJ	
Recent Price	30.98, as marked by JP Morgan on 11/28/08, this is a yield to maturity of approximately 28%
Description	This is the lowest AAA-rated class of a commercial mortgage-backed security backed by commercial mortgage loans originated by Morgan Stanley, Bear Stearns, Wells Fargo, and Principal Financial.
Rating	Aaa/AAA Moody's/Fitch
Credit Enhancement	10.5% -- meaning that the loan pool can suffer 10.5% loss before this class will suffer a loss.
Delinquency	0%. There have been no delinquencies in this transaction to date.

Loan Watchlist	The servicer's watchlist has two loans totaling 0.2% of the deal. Realpoint LLC (a third party CMBS monitoring firm) has five loans on its watchlist totaling 1.0% of the deal. From their watchlist, Realpoint expects a loss of <.06% of the deal.
Investor Interpretation	Securities rated AAA are actually carved out from established bright line tests. We include it here to suggest that, if this security can fail the test, then most CMBS of lower seniority will also fail the test, and this from a loan pool with 0% delinquencies.

Example 2. OHSF Financing Class D1	
Recent Price	22.92, as marked by JP Morgan on 11/28/08, this is a yield to maturity of approximately 40% and would violate the bright line test-- however see Pricing Issue discussion below
Description	This is the lowest BBB-rated class of a "market value CDO", a market-value-based financing on a portfolio of leveraged loans and high yield corporate bonds. It is managed by Oak Hill Advisors.
Rating	BBB S&P
Credit Enhancement	There is 7% equity value below this tranche – down from 17% at deal inception due to steep declines in loan and bond values. However, as of early December the manager is proposing injecting more equity into the transaction.
Pricing Issues	In mid November the manager launched a discount tender offer for up to 30% of the debt of this class at a price of 55. When no debt holders were willing to sell, the manager raised to offer to 65 and were able to get one small holder (\$2.5mm or 7% of the class) to sell at that price. A price of 65 would be a yield of approximately 13%.
Investor Interpretation	This is a vivid illustration of the magnitude of the liquidity premium and, in fact, incongruent price information being disseminated in the current market. There are no sellers of the security at a price of 65, and yet the price mark that we get from a reputable dealer is 23.

Example 3. Sandelman Finance CLO 2006-1 Class C	
Recent Price	22, as marked by Morgan Stanley on 11/28/08, this is a yield to maturity of approximately 33%
Description	This is a A-rated class in a CLO managed by Sandelman Partners. The collateral is at least 40% "middle market loans" – loans that are not broadly syndicated. However, an unusual fact is that 33% of the collateral is currently in cash (i.e., risk free). The manager sold loans in early 2008 in order to purchase loans later at a discount.

Rating	A2/A Moody's / S&P
Credit Enhancement	30% -- meaning that the loan pool can suffer 30% loss before this class will suffer a loss.
Defaults	0.8%. There is one credit in default, Pivotal Promontory. Estimated losses for that credit are estimated at 0.4% of the pool balance.
Investor Interpretation	There would appear to be little current evidence that this security will suffer a loss, particularly with only 67% of the pool in risk assets. Even if the cash component were re-lent, this would imply an extremely high default rate. As noted, there is less than 1% of the pool currently in default.

Our conclusion from the examples cited above and our inability to actually transact in any size at the price indications provided by market participants is that the credit markets are not functioning properly in the current environment and, therefore, cannot reflect reliable valuation information for accounting purposes. To force investors who are diligently monitoring the credit aspects of these securities to override the outcome of their thorough analysis with an arbitrary rule for impairment is a misapplication of accounting principles. Furthermore, the dangerous by-product of this accounting treatment is that it can easily perpetuate a downward spiral in the prices quoted for structured securities. The more market participants are forced to impair such securities, the more reluctant they are to buy such securities (even at prices that have no historical precedent). And, the more reluctance that permeates the investor bases for such securities, the more that prices will continue to fall.