



FEDERAL HOUSING FINANCE AGENCY
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Office of the Chief Accountant

January 16, 2009



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LETTER OF COMMENT NO. 68

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

File Reference: *Proposed FSP FAS 107a*

Dear Mr. Golden:

The Federal Housing Finance Agency (FHFA) is pleased to comment on FASB's proposed FASB Staff Position on FAS 107, *Disclosures about Fair Value of Financial Instruments*, (FSP FAS 107a). We serve as the supervisor of the Federal Home Loan Bank system and the supervisor and conservator of Fannie Mae and Freddie Mac. In discharging our responsibilities, we have a public policy interest in promoting transparency and disclosure in financial reporting as a means of fostering market discipline for both GSEs we regulate and for financial institutions more generally.

We support FASB's efforts to enhance disclosure regarding financial instruments. We note that FAS 107 was issued 18 years ago and that it could benefit from updating and enhancement, particularly given the current disruption in credit markets and controversy surrounding the disclosure of fair value information. We also note that under existing generally accepted accounting principles, multiple lots of a single security can have multiple measurement bases depending on whether specialized industry guidance is applicable or by elective intent of an entity's management. As FASB seeks to simplify the accounting for financial instruments, we believe that comparative disclosure of financial instruments at fair value and amortized cost would be useful to investors and other stakeholders. At the same time, explicit disclosure of incurred loss measurements for financial instruments could be useful to those stakeholders seeking to compare incurred loss to unrealized losses reflecting fair value. For example, such comparative disclosure would provide an indication of what an entity believes is the present value of a security's uncollectible cash flows versus the risk premiums and liquidity discounts implied by the security's fair value. The difference between incurred loss and unrealized fair value loss presumably is what management believes will be reflected in some fashion as investment yield during the entity's holding period. Such disclosure should spur additional

management discussion in the financial statements regarding its expectations for asset performance.

The following comments respond to specific questions posed in the exposure draft:

1. Will Requiring Disclosure Improve Quality and Comparability of Information?

In our view, requiring disclosure of impairment in its various guises under the mixed attribute accounting for financial instruments would be beneficial for investors and other stakeholders. We are uncertain, however, whether the proposed method for measuring incurred loss for impaired debt securities will provide a consistent, useful indicator. The proposal, which uses the discounted cash flow approach of FAS 114, may indicate impairment for prepayable securities that have fewer cash flows because their expected payoff is sooner than what was expected when the securities were purchased. Conversely, an extension of the securities' maturity would result in a "gain" as measured by the proposed technique as there would be more expected cash flow compared to when the securities were purchased. We associate the concept of incurred loss with a probable failure by a debt-security issuer to pay contractual cash flows, *i.e.*, probable default. We do not believe it was the intent of FASB to mix prepayment risk with credit risk, nor do we think it would be appropriate for preparers to aggregate the FAS 114-style measurement "gains" with incurred losses. If indeed FASB did intend to capture incurred credit losses, we recommend the disclosure requirement be amended, as it applies to prepayable assets, to financial instruments that are not expected to pay all cash flows according to contractual terms. An alternative would be to craft the guidance so as not to prescribe a particular method for measuring incurred loss. Rather, the disclosure requirement could simply mandate qualitative and quantitative disclosure of the entity's means of determining incurred loss. Such an approach might also make rapid adoption of the guidance by preparers more feasible.

2. Should the Disclosure Include Assets Measured at Fair Value and LOCOM?

We do not object to limiting the scope to financial assets that are not measured at fair value as entities may not have the technical means in place to measure incurred loss. It would seem objectionable to require implementing systems for a prescribed accounting measure if it were not used to manage the business. We do, however, support requiring the disclosure for assets carried at the lower of cost or fair value. With respect to loans held for sale, such data could be useful in evaluating the allocation of loan loss reserves for incurred losses that are not attributable to specific assets.

3. Would a *Pro Forma* Income Statement Improve Financial Reporting?

In our opinion the FAS 107 disclosure, which presents information about stocks of financial instruments at a point in time, would be greatly enhanced by information about flows, or changes in positions between two time points. Therefore, the *pro forma* income statement FASB is contemplating could significantly improve the usefulness of the fair value disclosure. Such additional disclosure could complement the existing disclosure requirements for financial instruments graded Level 3 under FAS 157.

5. Should the Disclosures Go Into Effect After December 15, 2008?

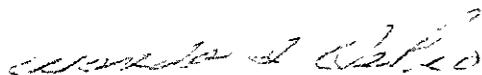
FHFA believes such disclosure would be timely and highly informative in the current economic environment. That said, we encourage FASB to be sensitive to views regarding the practicability

of implementation for 2009. Disclosure controls would need to be identified and weaknesses remediated in order to ensure reliable disclosures are made. At this point, we do not have a firm view regarding the capacity of entities under our supervision to comply in the timeframe FASB is contemplating. We do note, however, that historical cash flows will be needed to compute historical yield and such information may not be readily available for older vintage bonds. Furthermore, calculating an historical internal rate of return for each individual bond and feeding the result into a present value calculation of future cash flows is not a trivial task when performed on a large scale. Given these impediments, the timeframe FASB is considering putting the guidance in force further weighs against prescribing a FAS 114-style impairment measurement for impaired debt securities.

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In closing, we commend the FASB for its efforts to improve transparency of financial instruments during these challenging economic times and appreciate the opportunity to comment on this proposal.

Sincerely,



Wanda I. DeLeo
Senior Associate Director and Chief Accountant