

December 2, 2008

Via Email: director@fasb.org

Mr. Russell G. Golden FASB Technical Director Financial Accounting Standards Board 401 Merritt 7 Norwalk, CT 06856-5166

Dear Mr. Golden:

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LETTER OF COMMENT NO. 3

U.S. Central is a not-for-profit, cooperative wholesale corporate credit union. As a liquidity provider to its 26 member corporate credit unions, U.S. Central manages a balance sheet of approximately \$40 billion of high-quality debt securities. U.S. Central and its 26 members comprise the Corporate Network, providing liquidity, payment services and investment options to the nation's 8000 retail credit unions.

We have previously submitted comment letters to both the FASB and the SEC on issues associated with the exit price/liquidation value concept of FAS 157 for the buy-and-hold investor. We proposed minor modifications to fair value accounting, which are excerpted for your convenience as an Appendix to this letter. While our focus was directed to the definition of "fair value", our concerns have always been centered on how "fair value" affects the determination of other-than-temporary impairment charges.

The SEC, by letter dated October 14, 2008, asked FASB "to expeditiously address issues that have arisen in the application of the OTTI model in Statement 115."

We are encouraged by the momentum building in support of the Center for Audit Quality letter dated November 13, 2008. The suggested "enhancements" provide a practical model that we can support for debt securities. In particular, recognizing (expected) credit losses in net income is very similar to the net realizable value concept we proposed for debt securities when the investor has the intent and ability to hold to recovery or maturity.

The CAQ proposed solution is consistent with FAS 5, similar to whole loan accounting, and closer to international accounting standards. It would also reduce the earnings volatility caused by current OTTI guidance, where losses based on fair value are exacerbated by low market liquidity and extreme risk premiums—both of which are irrelevant unless the assets are *for sale*. Some critics have asserted it would be difficult to determine the expected credit losses. We disagree. We believe owners of debt securities already monitor these risks and could produce reasonable (and "auditable") estimates of these amounts. As an example, refer to Federal Home Loan Bank of Atlanta's third quarter results, whereby OTTI charges of \$87.3 *million* were recorded on expected credit losses of \$44 *thousand*, estimated to occur between 2025 and 2032.

Please give the CAQ proposal the serious consideration it deserves. It is essential that FASB act "expeditiously" to provide improved guidance on OTTI for year-end financial reporting.

Respectfully,

Kathryn E. Brick

Senior Vice President and Chief Financial Officer

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## **Appendix**

## Solution

We propose a simple solution. It parallels the treatment for loans, which are either held for sale or held for investment. Debt securities held for sale—whether they are classified as trading or AFS for which the investor cannot represent intent and ability to hold to recovery—should be valued at relevant market prices. In today's dislocated market, this includes the extreme liquidity risk premium in the FASB's example.

On the other hand, for debt securities for which the investor has represented intent and ability to hold (either HTM or AFS as currently interpreted), using fire-sale prices is contrary to the going concern presumption. HTM debt securities should continue to be held at amortized cost. But if other-than-temporary charges are required, the write-down should be based on realizable value, not a fire sale exit price. In the current, dislocated market, exit prices overstate losses which must then be reversed in subsequent periods as the securities pay their expected cash flows. AFS securities for which the investor represents intent and ability to hold to recovery should be adjusted for credit risk if necessary, but should not include the extreme liquidity risk premium of the FASB's example.

This proposed solution for fair value would also address the problems associated with OTTI.

## Alternative Solution

However, if the FASB and SEC are unwilling to make changes to the notion of exit values in extreme market conditions, Statement 115 could be amended to state that if impairment is judged to be other-than-temporary, the security should be written down to net realizable value (not fair value), based on expected principal and interest cash flows.

This alternative proposed solution avoids the problem of overstating losses described above.