

March 25, 2009



Via Email: director@fasb.org

LETTER OF COMMENT NO.

36

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

File Reference: Proposed FSP FAS 115-a, FAS 124-a, and EITF 99-20b

Dear Mr. Golden:

Southwest Corporate Federal Credit Union ("Southwest Corporate") appreciates this opportunity to comment on the proposed FASB Staff Position No. FAS 115-a, FAS 124-a, and EITF 99-20b *Recognition and Presentation of Other-Than-Temporary Impairments* (the "Proposed FSP").

Southwest Corporate is a federally chartered corporate credit union whose principal activity is to provide investment, financial and payment products to 1,500 federal and state-chartered natural person credit unions. Southwest Corporate manages a balance sheet of approximately \$11 billion, of which approximately \$4 billion is invested in marketable securities that are classified as available-for-sale. Southwest Corporate is a liquidity provider to natural person credit unions. As such, our investments are generally comprised of marketable securities instead of a portfolio of unsecuritized loans to individuals. Southwest Corporate is a buy and hold institution; however, we historically classify all securities as available-for-sale in order to fulfill our role as a liquidity provider.

Executive Summary

- Southwest Corporate supports recording other-than-temporary impairments through the income statement for *only* the projected credit loss. This is consistent with loan impairments and as discussed below is a significant improvement to current generally accepted accounting principles (GAAP).
- Southwest Corporate believes it is **critical** to allow entities to early adopt this standard to 2008 audited financial statements if they believe it will have a material impact on their financial reports. Southwest Corporate believes this is consistent with the accounting for a change in accounting principle as discussed in FASB Statement No. 154 *Accounting Changes and Error Corrections*. Requiring a prospective adoption will result in a needless reduction of capital when the

accounting principles are changing in the next quarter. Allowing entities to choose retroactive application is a responsible and reasonable action and is supported by existing GAAP.

- Southwest Corporate believes that upon adoption, entities should be able to reverse the non-credit portion of previous impairments. This will allow consistent and comparable treatment of securities held by an entity and comparability among entities.
- Southwest Corporate appreciates FASB's consideration of these changes.

Southwest Corporate has provided comment letters to both FASB and the SEC. These comment letters have consistently supported recording other-than-temporary impairments based on credit losses which is similar to accounting for unsecured loans. In December of 2008, Southwest Corporate endorsed the approach recommended by the PCAOB which would record impairments only to credit loss with the remaining portion included in other comprehensive income. Southwest Corporate was encouraged that the SEC also recommended changes to the impairment model in its December report to Congress.

FASB had the opportunity to correct the accounting for impairments when FSP EITF 99-20-1 *Amendment to Impairment Guidance of EITF Issue 99-20* was issued in January of 2009 but chose to address only issues arising from the application of EITF 99-20. Had FASB taken action in December, entities could have applied this accounting to year-end financial reporting. Southwest Corporate appreciates that FASB is taking action now to correct the accounting but believes it is imperative that FASB permit retroactive adoption to 2008.

1. This Proposed FSP would require entities to separate (and present separately on the statement of earnings or "performance indicator") an other-than-temporary impairment of a debt security into two components when there are credit losses associated with an impaired debt security for which management asserts that it does not have the intent to sell the security, and it is more likely than not that it will not have to sell the security before recovery of its cost basis. The two components would be (a) the credit component and (b) the noncredit component (residual related to other factors). Does this separate presentation provide decision-useful information?

This is a significant improvement to current GAAP and aligns accounting for security impairments more closely with accounting for loans. Southwest Corporate has been a strong advocate of recording impairments to credit loss and has responded to several prior exposure drafts recommending similar impairment accounting treatment for securitized loans and unsecuritized loans.

There are several reasons why Southwest Corporate believes the Proposed FSP is improved GAAP. These reasons are based on the following FASB Concept Statements for which all principles-based standards should be derived.

Concept Statement 1 *Objectives of Financial Reporting by Business Enterprises*

• **Information Useful in Investment and Credit Decisions**

“This statement indicates that financial reporting should provide information that is useful to present and potential investors, creditors and other users in making rational investment, credit and similar decisions.”

Allowing entities that do not intend to sell securities to record impairments to credit losses provides more useful information to users of the financial reports. This accounting is more understandable as it presents results which are based on the intrinsic value of the holdings. Recording the recoveries of the non-credit losses in future periods distorts future earnings and makes the reports less useful to users.

Of notable importance is that the fair value of the holdings is still provided on the face of the balance sheet for available-for-sale securities, thus adding further transparency for users of financial information.

• **Enterprise Performance and Earnings**

“This statement indicates that financial reporting should provide information about an enterprise’s financial performance during a period.” “The statement also notes that accrual accounting attempts to record the financial effects on an enterprise in the periods in which those transactions, events, and circumstances occur.”

Recording the non-credit component in income violates this concept for entities that do not intend to sell the impaired securities. It is also difficult to estimate an entity’s long-term earnings potential in both current periods when the non-credit component is recorded in income and in future periods when it is reversed through accretion income. Thus, allowing write-downs to credit losses prevents the gross-up of future earnings based on accretion income which does not reflect the true economic performance of the entity in those future periods.

FASB should consider allowing reversals of impairment recorded in earnings related to credit losses in the future if significant assumptions change.

The proposed FSP satisfies the criteria for providing better information about an enterprise’s performance and earnings potential than the current impairment guidance.

Concept Statement 2 *Qualitative Characteristics of Accounting Information*

- **Relevance**

“Relevant accounting information is capable of making a difference in a decision by helping users to form predictions about the outcomes of past, present, and future events to confirm or correct prior expectations.”

Recording other-than-temporary impairments to fair value is only relevant if the entity intends to sell the security. The unprecedented market conditions that currently exist highlight the inherent flaws in fair value accounting as a basis for recognizing other-than-temporary impairments. Under current GAAP, the non-credit portion of the impairment will be recorded as net interest income in future periods as the securities pay down. This additional income distorts the future performance of the enterprise by making the enterprise appear more profitable due to recording prior reductions of retained earnings.

Entities will be required to continue to monitor securities to determine if additional other-than-temporary impairments are required. It is more relevant to record additional impairments to credit losses if the performance of the underlying collateral deteriorates in the future, as well as to reverse the impairment related to credit losses in the future if the underlying collateral improves.

The fair value of the securities continues to be provided to the users of the financial statements and thus, the Proposed FSP provides more relevant information to the users of financial statements than the current impairment guidance.

- **Reliability**

One of the tenets of reliability is neutrality. “A neutral choice between accounting alternatives is free from bias towards a predetermined result.”

Recording other-than-temporary impairments to fair value has a bias toward selling a security, which in the current distressed market implies a bias toward liquidation accounting. Thus, recording other-than-temporary impairments to credit losses is more neutral than the current practice.

Additionally, entities should be allowed to apply the Proposed FSP to all securities that have previously been impaired. They should be able to reverse the non-credit portion of the impairment at the time of adoption. This will provide a neutral, consistent application to **all** securities which are held by the entities. FASB should conclude that this is an improvement to GAAP and not penalize entities that took impairments to fair value in earlier periods.

- **Comparability and Consistency**

“Information about a particular enterprise gains greatly in usefulness if it can be compared with similar information about other enterprises and with similar information about the same enterprise for some other period or some other point in time. Comparability between enterprises and consistency in the application of methods over time increases the informational value of comparisons of relative economic opportunities or performance.”

The application of the Proposed FSP will allow consistent and comparable treatment between unsecuritized loans and securitized loans. This is considered a significant improvement to current practice. Southwest Corporate believes that FASB should ensure comparability and consistency of financial statements and allow entities that have previously recorded other-than-temporary impairments to reverse the non-credit portion at the time of adoption. This will enhance consistency and comparability within an enterprise, as well as among enterprises. Retroactive application also provides comparability and consistency among periods.

- **Materiality**

Southwest Corporate notes that the Board considered whether insignificant credit losses should be disregarded. Southwest Corporate believes that insignificant credit losses should not be required to be recorded as other-than-temporary impairments. In applying the Proposed FSP, an insignificant credit loss would be recorded in income. Southwest Corporate does not believe that recording an insignificant credit loss would provide relevant or useful information for securities that are classified as available-for-sale as the unrealized loss is already recorded in accumulated other comprehensive income. Not recording an insignificant credit loss would also have an insignificant impact on net income for securities which are classified as either available-for-sale or held-to-maturity.

- **Understandability**

As discussed above, Southwest Corporate believes that the Proposed FSP meets the criteria established under Concept Statements 1 and 2 and improves the understandability of financial statements. It is a significant improvement to current practice.

2. This Proposed FSP would require that the credit component of the other-than temporary impairment of a debt security be determined by the reporting entity using its best estimate of the amount of the impairment that relates to an increase in the credit risk associated with the specific instrument. One way of estimating that amount is to consider the measurement methodology described in paragraphs 12–16 of FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan*. For debt securities that are beneficial interests in securitized financial assets within the scope of Issue 99-20, the amount of the total impairment related to credit losses would be determined by considering the guidance in paragraph 12(b) of Issue 99-20. Do

you believe this guidance is clear and operational? Do you agree with the requirement to recognize the credit component of an other-than-temporary impairment in income and the remaining portion in other comprehensive income? Under what circumstances should the remaining portion be recognized in earnings?

Southwest Corporate believes the guidance in the Proposed FSP is clear and operational. We have the ability to apply this guidance retroactively to 2008 financial statements. Southwest Corporate agrees that a principle based approach is required for the calculation of credit losses. We are appreciative that FASB is not prescribing a methodology but indicating that "*One way of estimating (emphasis added)* that amount would be to consider the measurement methodology described in paragraphs 12–16 of FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan.*"

This Proposed FSP which would allow the recognition of the credit component of an other-than-temporary impairment in income and the remaining portion in other comprehensive income is a significant improvement to current GAAP. Accounting for security impairments is aligned more closely with accounting for loans. Southwest Corporate has responded to several prior exposure drafts recommending similar impairment treatment for securitized loans as is given to unsecuritized loans. This change improves the comparability of financial statement components (loans versus securities) within an institution as well as among institutions that hold securitized loans instead of unsecuritized loans.

As discussed above, the current practice distorts current performance for institutions that buy and hold securities (regardless of classification). The current practice requires an adjustment to fair value in the current period and then allows recovery in future periods for the non-credit portion of the impairment. Future net income is materially distorted by the recovery of the non-credit portion. These future "earnings" are not real but only a recapture of prior write-offs and could result in entities appearing healthier and could mitigate true economic indicators of performance. One of the basic tenets in accounting should be neutrality of the standard. The current standard is not neutral to entities which buy and hold securities.

Southwest Corporate believes that the remaining portion (non-credit loss) should be recorded in earnings if an entity plans to sell a security.

3. This Proposed FSP modifies the current indicator that, to avoid considering an impairment to be other than temporary, management must assert that it has both the intent and the ability to hold an impaired security for a period of time sufficient to allow for any anticipated recovery in fair value. The Board believes that compared to current requirements, it is more operational for management to assert that (a) it does not have the intent to sell the security and (b) it is more likely than not that it

will not have to sell the security before its recovery. Does this modification make this aspect of the other-than-temporary impairment assessment more operational (the remaining factors discussed in FSP FAS 115-1/FAS 124-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*, would remain unchanged)? Should this modification apply to both debt and equity securities? Will this change result in a significant change to the assessment of whether an equity security is other-than-temporarily impaired?

Southwest Corporate agrees that it is more operational to assert that management does not intend to sell a security and is more likely than not to hold a security to recovery. Southwest Corporate is a buy and hold institution; therefore, this will not have a significant change to our assessment.

Southwest Corporate does not hold equity securities; however, we believe fundamentally that there should not be multiple impairment models.

5. Is the proposed effective date of interim and annual periods after March 15, 2009, operational?

FASB should permit a retroactive application of this guidance to December 31, 2008 financial statements. Entities that find retroactive application impractical could elect to apply the guidance on a prospective basis. FASB Statement No. 154, *Accounting Changes and Error Corrections*, indicates that a change in accounting principle be applied as of the beginning of the earliest period for which retroactive application is practicable. The guidance in the Proposed FSP is clearly a change in accounting principle. Allowing a retrospective application would be a responsible action by FASB and would have a significant impact to financial reports. FASB had the opportunity to take this action in December of 2008 which would have impacted year-end financial reports. Entities should be permitted to adopt this retroactively if they choose. This will be particularly beneficial for entities that have not issued audited financial statements. Southwest Corporate views retroactive application as critical.

The Proposed FSP is a significant improvement to current guidance. Southwest Corporate believes that entities should be permitted to apply this guidance retroactively. FASB should also allow the non-credit portion of prior impairments at the time of adoption to be reversed to other comprehensive income. This will result in a significant improvement in the consistency and comparability between entities. FASB should consider allowing reversals of credit impairments if assumptions significantly change in the future.

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I appreciate your attention to this matter and to the points raised in this letter. I welcome a discussion at your convenience. Please feel free to contact me at 214-703-7890.

Sincerely,

Melissa Wardell

Melissa Wardell
SVP-Chief Financial Officer
Southwest Corporate Federal Credit Union