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LETTER OF COMMENT NO. 44

Technical Director – File Reference **1530-100**
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

Exposure Draft: Accounting for Financial Guarantee Insurance Contracts

Dear Technical Director:

We appreciate the opportunity to comment on the Financial Accounting Standards Board's ("FASB" or "Board") Exposure Draft on "Accounting for Financial Guarantee Insurance Contracts". While we are supportive of the Board's objectives for reducing diversity in the way financial guarantee insurance contracts are accounted for, we are equally concerned about some specific provisions of the standard.

Fitch Ratings (Fitch) is a leading global rating agency committed to providing the world's credit markets with independent, timely and prospective credit opinions. Fitch maintains insurer financial strength ratings on over two-thousand insurance companies world-wide, including eight financial guarantors based in the U.S. Fitch's corporate finance ratings make use of both qualitative and quantitative analyses to assess the business and financial risks of fixed-income issuers. Therefore, Fitch directly relies on the financial statements and that reliance places us in an informed position to comment on information we believe is useful and crucial in the credit evaluation process, which is a critical component of efficient capital markets.

Exposure Draft Comments

As stated above, we are supportive of the Board's objectives for reducing diversity in the way a financial guarantor's insurance contracts are accounted for. We note however that the proposal only addresses accounting for insured liabilities provided by a financial guarantor in "financial guaranty" form but not in "credit default swap" (CDS) form. Because the risks undertaken by the guarantor are similar for a financial guaranty and CDS transaction, we believe that the accounting treatment for these two forms of providing credit enhancement should be aligned.

Additionally we have some concern about the following four specific provisions of the Exposure Draft:

1) We support the Board's intention that financial guarantors recognize premium revenue over the period of the contract in proportion to the insured contractual payments made by the issuer of the insured financial obligation. However, we strongly believe that the reduction of exposure due to the passage of time should be firmly embedded in any revenue recognition model adopted. This point is illustrated in the table in Appendix I entitled "Corporate Finance- 1-10 Year Mean Cumulative Default Rates". As illustrated in the table, bonds with shorter terms to maturity have a significantly lower probability of default than bonds with longer terms to maturity. Specifically, the proposed guidance will require revenues to be recognized at maturity for contracts whereby the contractual payments are made only at maturity (e.g. zero coupon bonds). Fitch believes that an alternative recognition approach should be adopted for such obligations. We suggest that revenue recognition of insurance contracts that guarantee obligations similar to zero coupon bonds should be based on a straight-line recognition of premium revenue over the contractual term of the bond being insured.

2) With regard to a financial obligation where, due to prepayments, the actual term of the exposure is usually shorter than the contractual term (for example, residential mortgage backed securities), Fitch believes that revenue recognition based on expected cash flows rather than contractual cash flows capture the economic reality of the financial guarantee. We understand that this approach may cede to management a great deal of flexibility in what is termed "expected cash flow", however, we believe that the basis of such classification should be a required disclosure in the accompanying notes to financial statements. Alternatively, standard maturity terms based on readily observable information about prepayments can be established for certain structured products in order to prevent inconsistencies in the implementation of the expected life approach to recognizing revenues.

3) We agree with the Board's approach to contracts that relate to insured obligations that are called or refunded before the scheduled maturity of the obligation – any nonrefundable unearned premium revenue related to that contract is immediately recognized as premium revenue. However, we disagree with the Board's approach to accounting for instances whereby the called instrument is replaced by a new financial obligation insured by the same financial guarantor. The Board proposes that any premium differential between the premium charged on the new financial obligation and the premium charged on a standalone transaction be recognized in current income. Fitch believes that the basis for computing any such differential would be highly subjective and not based on readily available data. Therefore, the volatility imposed on the financial statements based on this calculation would not enhance the transparency of the revenue line item in the income statement.

4) Lastly, Fitch generally views the Board's proposed claim liability methodology as reasonable and believes that a consistent approach to claim liability across the industry will facilitate financial statement comparability. That said, Fitch does not agree that a

claim liability should be recognized only after the expected loss exceeds the unearned premium revenue liability for a given contract. Fitch believes financial statement transparency would be enhanced if claim liabilities are recognized with the first dollar of expected loss, not only after the expected cash flow of the loss exceeds the associated unearned premium revenue liability.

We would be happy to answer any questions regarding our comments and look forward to discussing these comments with the Board at the appropriate time. We would also welcome an invitation to the roundtable discussion tentatively scheduled for July 16, 2007.

Yours sincerely,

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Appendix I

Corporate Finance – 1-10 Year Mean Cumulative Default Rates

Year	1	2	3	4	5	6	7	8	9	10
AAA	0.00%	0.00%	0.01%	0.06%	0.14%	0.20%	0.28%	0.38%	0.41%	0.43%
AA+	0.00%	0.00%	0.01%	0.08%	0.18%	0.25%	0.33%	0.45%	0.52%	0.60%
AA	0.00%	0.00%	0.01%	0.10%	0.22%	0.29%	0.39%	0.52%	0.63%	0.76%
AA-	0.03%	0.09%	0.18%	0.29%	0.41%	0.55%	0.65%	0.72%	0.77%	0.88%
A+	0.03%	0.10%	0.25%	0.41%	0.53%	0.68%	0.79%	0.93%	1.12%	1.35%
A	0.04%	0.14%	0.26%	0.42%	0.63%	0.84%	1.03%	1.32%	1.60%	1.84%
A-	0.04%	0.22%	0.41%	0.59%	0.80%	1.07%	1.44%	1.68%	1.94%	2.16%
BBB+	0.26%	0.74%	1.25%	1.73%	2.21%	2.68%	3.05%	3.33%	3.68%	3.97%
BBB	0.28%	0.81%	1.29%	1.79%	2.29%	2.93%	3.57%	4.27%	4.92%	5.80%
BBB-	0.46%	1.32%	2.23%	3.47%	4.70%	5.84%	6.85%	7.71%	8.33%	9.08%
BB+	0.67%	2.14%	4.03%	5.86%	7.45%	9.25%	10.62%	11.64%	12.66%	13.56%
BB	1.24%	3.58%	5.71%	7.86%	10.13%	12.05%	13.85%	15.33%	16.69%	17.45%
BB-	2.16%	6.05%	10.36%	14.49%	18.18%	21.69%	24.66%	27.56%	30.30%	32.56%
B+	3.21%	9.17%	14.92%	20.06%	24.45%	28.32%	32.28%	35.42%	38.18%	40.74%
B	7.77%	16.46%	23.31%	28.49%	32.38%	35.21%	37.14%	38.88%	40.64%	42.42%
B-	12.28%	22.69%	31.05%	37.21%	42.09%	46.05%	49.24%	51.99%	53.57%	54.38%
CCC	26.96%	35.76%	46.78%	52.79%	57.30%	60.27%	62.54%	65.19%	67.18%	69.33%

Source: The Fitch Matrix Financial Guaranty Capital Model, January 9, 2007
Available at www.fitchratings.com