Office of the Comptroller of the Currency Board of Governors of the Federal Reserve System Federal Deposit Insurance Corporation National Credit Union Administration Office of Thrift Supervision

April 1, 2009

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

LETTER OF COMMENT NO. 328

Re: File Reference: Proposed FSP FAS 157-e

Dear Mr. Golden:

We are pleased to submit comments on behalf of the staffs of the five federal financial institution regulatory agencies on the proposed FASB Staff Position (FSP), *Determining Whether a Market Is Not Active and a Transaction Is Not Distressed.* We appreciate the FASB's efforts to further clarify fair value measurements for financial assets in this difficult environment.

The agencies support the FASB's efforts to further clarify fair value measurement because an overreliance on using the most recent transaction price in an illiquid market without significant adjustment as the basis for estimating fair value may result in overly conservative values that reflect distressed or forced sales. Accordingly, guidance that will improve fair valuation practices and assist preparers and auditors in achieving the fair value measurement objective of Statement of Financial Accounting Standards No. 157, Fair Value Measurements (FAS 157), is warranted. However, we are concerned that this proposal does not strike an appropriate balance. Therefore, we offer the following comments and recommendations to improve the proposal.

Although paragraph 7 of FAS 157 states that an orderly transaction is "not a forced transaction (for example, a forced liquidation or distressed sale)," the standard provides limited guidance on the types of transactions that would be considered forced or distressed. Paragraphs 17 and C25 of FAS 157 note that a transaction may be a forced transaction if the seller is experiencing financial difficulty. However, we believe the proposed FSP's rebuttable presumption that a transaction is distressed when the market for an asset is not active and both factors identified in paragraph 13 are not present should be removed. There is no reasonable basis for presuming that each transaction in an inactive market is or is not distressed. As a consequence, a presumption that transactions in inactive markets are distressed could provide an incentive for an entity to

inappropriately ignore reasonable market data that may be relevant in determining a fair value measurement.

We support the notion that fair value is not the last transaction price when that transaction price does not meet the definition of fair value (e.g., if it is a distressed transaction), and we believe that reasonable judgment must be exercised by preparers and appropriately documented and disclosed. Appropriately weighing all available evidence, rather than an explicit rebuttable presumption, would help to ensure an appropriate fair value measurement based on the applicable facts and circumstances specific to a transaction in an inactive market.

To assist preparers and auditors in considering all available evidence, providing discussions or examples of situations that represent, or may represent, forced sales or distressed transactions would be beneficial. Guidance could be provided on the distinction between a distressed seller and a distressed transaction and on various types of transactions that are often cited as distressed, such as a secured party's sale of collateral in response to a margin call. In this regard, we would also appreciate further guidance on whether sales of financial assets by a bankruptcy trustee or receiver (such as the Federal Deposit Insurance Corporation [FDIC] and the National Credit Union Administration) when exercising its fiduciary responsibility to sell the assets of a debtor in liquidation or a failed insured depository institution should be treated as distressed transactions. In discharging its responsibility to convert assets to settle claims of creditors, the trustee or receiver may not be a market participant, as described in paragraph 10 of FAS 157, because it is compelled to enter into transactions to dispose of assets in response to legal requirements governing its conduct and activities. For example, when the FDIC is acting as a liquidator, it does not pursue a holding strategy for failed bank assets; rather it seeks to dispose of the assets as quickly as possible as is consistent with its statutory duties. This policy is driven in part by the FDIC's experience that many types of assets deteriorate in value rapidly while in receivership.

We also strongly recommend that the FASB work with the Public Company Accounting Oversight Board and the American Institute of Certified Public Accountants to ensure that auditing standards and guidance reinforce the concepts in the final FSP, including fair valuations in illiquid markets. In this regard, when rendering a determination on management's judgment, an auditor must also exercise significant judgment and consider all available evidence and not just the last transaction price.

The example in paragraph A32 of the proposed FSP provides useful guidance for determining an appropriate discount rate. However, because the range of possible rates of return presented is narrow, it does not adequately reflect the wide range currently existing in practice from the perspective of willing buyers and sellers for many financial assets in markets that are not active. When the discount rate range is very wide, the midpoint, which was selected in the example, may not be appropriate, but it may, by default, become the discount rate upon which preparers and auditors agree to compromise. Further, given the importance of the selected discount rate to the preparer's ultimate fair value estimate, the FASB should consider requiring discount rate disclosures.

We encourage the FASB to provide additional discussions or examples of how reasonable judgment can be used in arriving at fair value, including utilization as appropriate of the

International Accounting Standards Board Expert Advisory Panel paper, *Measuring and disclosing the fair value of financial instruments in markets that are no longer active*. This paper, which was developed based on extensive input, has been helpful in providing additional guidance in this area.

In addition, the FSP would amend FAS 157 by adding a new paragraph 29A. Step 2 in this new paragraph discusses two factors that should be considered when assessing whether a quoted price is associated with a distressed transaction. The first factor says that "[t]here was a period before the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets or liabilities (for example, there was not a regulatory requirement to sell)." We recommend replacing the word "regulatory" with "legal" because it has broader applicability.

Finally, paragraph 17 of the proposed FSP states that "[r]evisions resulting from a change in the valuation technique or its application shall be accounted for as a change in accounting estimate." With respect to investment securities within the scope of Statement of Financial Accounting Standards No. 115, Accounting for Certain Investments in Debt and Equity Securities, we encourage the FASB to provide guidance that will eliminate potential confusion by clarifying that such revisions are not a "rare occurrence" or an "isolated, nonrecurring, and unusual" event for purposes of reclassifying securities to or from the trading portfolio or from the held-to-maturity portfolio, respectively.

The agencies appreciate your consideration of the above comments. We would be pleased to discuss our views with you further.

Sincerely,

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