



May 22, 2013

Technical Director  
Financial Accounting Standards Board  
401 Merritt 7  
P.O. Box 5116  
Norwalk, CT 06856-5116  
**Delivered via Email to director@fasb.org**

RE: Credit Losses (Subtopic 825-15)

Dear Director:

As FASB continues to work on its credit losses proposal, it is critical that FASB understand the unique structure of credit unions. Credit unions are member-owned, not-for-profit financial cooperatives that operate for the purpose of promoting thrift, providing credit, and providing other financial services at competitive rates. In addition, credit unions are unique from other financial institutions in that their enabling statute, the Federal Credit Union Act, limits net worth to retained earnings only. Further, this statutory limitation restricts the ability of the National Credit Union Administration (NCUA)—the prudential regulator of federally chartered credit unions and insurer of most state and all federally chartered credit unions—to adjust its regulations in response to changes in accounting standards, as is possible for other federal financial regulators.

The proposal would require credit unions to provide information that is not relevant to the primary users of credit unions' financial statements, who are the NCUA and state credit union regulators. The financial statement users of a credit union are so very different from those of a bank, including both public and private.

FASB's stated intent behind issuing the proposed changes is that the current impairment methodology does not allow for the timely recognition of credit losses. We do not agree with this. We also do not believe the proposed approach would have been effective at preventing the extent of credit losses experienced over the past several years. This is because we do not believe it is possible to accurately predict the extent and timing of the credit events that led to such widespread losses within the financial sector.

While we oppose much of the proposal, we do support the proposed changes regarding mergers/business combinations. Specifically, we agree with the proposed treatment that would bring the allowance of the target entity over to the continuing entity in a merger situation.

As I see it, the most problematic areas as it relates to credit unions, include:

- 1) The proposal would require credit unions to recognize on the balance sheet, current loss expectations in the Allowance for Loan and Lease Losses (ALLL). Thus, upon becoming effective, the proposed changes would cause an immediate and drastic increase to the ALLL of credit unions that have financial assets and liabilities within the (broad) scope of the proposal. This increase, which we expect will double or even triple current ALLLs, will result directly in a reduction in many credit unions' retained earnings.

- 2) Further, a decrease in earnings can lead to a reduced capital ratio, which can trigger prompt corrective action (PCA) implications for numerous credit unions that currently do not have PCA concerns.
- 3) The proposed current expected credit loss (CECL) approach has the potential to lead to quarterly adjustments in expected loss projections, possibly resulting in more volatility in provision expense and earnings.
- 4) Another possible result of the proposal is that reporting entities could take large one-time charges at first signs of distress in their loan portfolios, and then look for opportunities to smooth earnings volatility over time through reserve releases or reverse provisions.
- 5) One result of the proposal that is certain is that it will require credit unions to expend extensive financial and technical resources to even begin to comply with the changes proposed. The costs of any such expenditure will be borne by credit unions' member owners. The proposal attempts to address the problems of a few financial institutions—albeit some extremely large financial institutions—that misled or simply did not understand the credit quality of complex CMOs and MBSs by proposing far-reaching changes that will severely impact all financial institutions, including credit unions that did not cause the financial crisis.
- 6) Unfortunately, the proposed changes could ultimately result in the consolidation of credit unions that are unable to comply with these changes. Such a result would not only affect the members of those credit unions directly involved, but would affect the larger financial services marketplace by reducing consumer financial options.

The proposed CECL model effectively requires entities to predict/forecast the extent and timing of future losses. Predicting such losses with any degree of accuracy will be extremely challenging, even for an entity with adequate data sets and modeling capability. Further, attempting to predict credit loss for the life of a loan will inherently be affected by the subjectivity of and assumptions made by the reporting entity.

In regard to the data necessary to conduct such modeling, even the largest financial institutions have indicated that they do not have adequate information on this data and that it will take years (some estimating four to five years) to obtain. Further, since smaller financial institutions will require even more time to obtain such data, these institutions will default to relying on their larger counterparts peer information, which will have a lag of at least six to nine months. In addition, even once smaller institutions obtain adequate data; it will take another three to four years for these institutions to become comfortable with the required modeling.

The proposed CECL model is inconsistent with the accounting principle of matching, which states that expenses should be recorded in the same period as the revenues that relate to those expenses. The proposal is inconsistent since it requires expected future loan losses to be recorded immediately. In addition to its impact on the reporting entity, this inconsistency will likely cause challenges/trepidation within the audit community.

While FASB maintains its intention to achieve a convergence of standards with the International Accounting Standards Board (IASB), including on credit losses, it is unclear how this will occur since the IASB's and FASB's credit losses proposals are so very different. Unlike the FASB proposal, which does not include a trigger for recognizing certain losses, the IASB proposal provides that an entity would only recognize a portion of expected credit losses until a specific recognition trigger has been met. The IASB's credit losses model utilizes the following two-bucket approach:

- a. 12-month expected credit loss (Bucket 1): Only requires full expected loss recognition when there is a significant increase in credit risk since origination or acquisition.
- b. Lifetime expected credit loss (Bucket 2): For all other assets, credit losses are recorded based on the probability of a default occurring in the next twelve months.

We believe it would be inappropriate to apply the proposed changes to credit unions, based on their unique structure as private, not-for-profit, cooperatively owned, financial institutions. As noted above, the primary

user of a credit union's financial statements is its regulator, which is not likely to benefit from the proposed changes since it already has a well-developed understanding of the operations of the credit unions it regulates.

We urge FASB to work closely with the federal financial regulatory agencies throughout the remainder of the standard-setting process, and we encourage such collaboration to continue, particularly with NCUA in light of the unique structure of credit unions.

We ask FASB to consider a credit impairment approach that is more in-line with the proposed IASB model, particularly the aspect of the IASB's model that uses a twelve-month forecast period.

We ask FASB to clarify what is meant by the term "lifetime expected losses," which is used throughout the proposal but not explicitly defined.

If FASB moves forward with this or a variation of this proposal, it is crucial that there be an adequate phase-in/transition period for credit unions. Further, we urge FASB to delay the effective date of a final credit losses standard by at least three years for non-public reporting entities, including credit unions.

I conclude by saying that the current FASB rules are more than adequate in providing a fair picture of the financial stability of a credit lender and therefore, respectfully ask that this proposal be withdraw. Thank you for your time.

Sincerely,

Cheryl Gibson  
President/CEO  
AAFES Federal Credit Union