



VIA Electronic Mail

December 5, 2007



Mr. Robert H. Herz  
Chairman  
Financial Accounting Standards Board  
401 Merritt 7  
Norwalk, CT 06856

LETTER OF COMMENT NO. 15

Dear Mr. Herz:

The Mortgage Bankers Association<sup>1</sup> (MBA) is writing to request the Board's assistance in addressing an operational impediment to the likelihood that hundreds of thousands of mortgage loans might need to be modified over the next two years. More specifically, MBA members report that they do not have the systems capability, and are unlikely to be able to obtain the capability, to evaluate huge volumes of modified loans under FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan*. MBA is greatly concerned that without some relief in the form of additional guidance from the FASB, mortgage lenders would be in the untenable position of having to modify loans that they could not account for in conformance with generally accepted accounting principles (GAAP).

As the FASB is undoubtedly aware, the mortgage banking industry is under tremendous pressure to modify loans, particularly adjustable rate mortgage (ARM) loans with initial, below-market fixed rates, to avoid a further escalation of mortgage defaults and foreclosures in this country. In recent months, MBA has been working closely with regulators, legislators, consumer advocates and others in seeking viable alternatives for modifying great numbers of loans as quickly as possible. In considering the many challenges associated with the prospect of unprecedented loan modifications, MBA has identified the guidance in FAS 114 as an obstacle that most companies could not overcome.

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<sup>1</sup> The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 400,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 3,000 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: [www.mortgagebankers.org](http://www.mortgagebankers.org).

Specifically, FAS 114 requires modified smaller balance, homogeneous residential mortgage loans that represent troubled debt restructurings to be evaluated for impairment on a loan-by-loan basis although loans that share risk characteristics may be evaluated on an aggregated basis.<sup>2</sup> Under either scenario, a mortgage lender would likely be required to measure impairments of the loans using discounted cash flow analyses because, in many cases, the values of the underlying collateral and observable market prices for the loans would be unobtainable or unavailable timely. The vast majority of MBA members, however, do not have the systems capability to project the cash inflows to be received on enormous numbers of loans either initially or on an ongoing basis.

This is because mortgage banking companies have not had the need to project cash flows on large numbers of modified loans until now. Generally speaking, mortgage banking companies traditionally have held relatively few loans in portfolio. Their loans in portfolio, however, have increased in recent months as the secondary market for many "subprime" and other loans has diminished dramatically. MBA members have been evaluating those loans for impairment under FAS 5, *Accounting for Contingencies*, which requires the establishment of loan loss allowances for credit losses that are probable of occurring and can be reasonably estimated as of the reporting date.

Given the pressures being brought to bear on lenders to undertake mass modifications, MBA believes they should be permitted to continue to apply the guidance in FAS 5 to modified smaller balance, homogeneous loans that represent troubled debt restructurings because:

- The guidance in FAS 114 was never intended to be applied on a global scale as indicated by the fact that the Board specifically excluded smaller balance, homogeneous loans from the scope of the Statement. MBA believes the Board's decision to exclude these loans from the scope of FAS 114 was motivated primarily by a desire to make the Statement practical to apply. Consequently, MBA believes modified residential mortgage loans would not have been included in the Statement if the Board had known that hundreds of thousands of them could be subject to evaluation within the same reporting periods at substantial cost to lenders for arguably no benefit in terms of improved financial information;
- FAS 5 provides for a cost effective approach to accurately measuring probable credit losses on large volumes of loans which is consistent with the objective of a loan modification which is to reduce the prospect of future credit losses. By contrast, a FAS 114 measurement approach would result in the recognition of losses related to a reduction in projected interest cash flows (where a modification involved a reduction in the interest rate) *unrelated to estimated credit losses at the reporting date*;
- FAS 5 would produce reliable balances for loans using a methodology that is consistent with the cost basis measurement approach for loans that are classified as held for investment under FAS 65, *Accounting for Certain Mortgage Banking Activities*;

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<sup>2</sup> See paragraph 12 of FAS 114.

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- Last, but not least, mortgage lenders have the systems and procedures necessary to measure impairments under FAS 5, but not FAS 114, at this time.

For these reasons, MBA respectfully requests that the Board release some guidance that provides relief from the requirements of FAS 114 to modified smaller balance, homogeneous loans that represent troubled debt restructurings. MBA is very concerned that without relief mortgage lenders on an industry-wide basis could be forced to issue qualified financial statements. As lenders are anticipating undertaking mass modifications beginning next year, they are anxious to learn whether the Board believes their concerns with respect to FAS 114 can be addressed.

MBA greatly appreciates the opportunity to share our views and thoughts on important accounting matters with you. If you have questions about our request, please contact Alison Utermohlen, Staff Representative to MBA's Financial Management Committee, at [autermohlen@mortgagebankers.org](mailto:autermohlen@mortgagebankers.org) or (202) 557-2864.

Most sincerely,



Jonathan L. Kempner  
President and Chief Executive Officer

Cc: Conrad W. Hewitt, Chief Accountant, Securities and Exchange Commission