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April 1, 2011

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

***Re: File Reference No. 2011-150***

Dear Director:

The Pennsylvania Credit Union Association (PCUA) appreciates this opportunity to comment on the Financial Accounting Standards Board's (FASB) Supplementary Document, *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities – Impairment*. PCUA is a state-wide trade organization that represents a majority of the 545 credit unions located in the Commonwealth of Pennsylvania.

PCUA consulted with its Regulatory Review Committee and State Credit Union Advisory Committee (the Committees) in order to provide comments on the proposed Supplementary Document. The combined Committees consists of twenty-two (22) credit union CEOs who lead the management teams of Pennsylvania's federal and state-chartered credit unions. Members of the Committees also represent credit unions of all asset sizes. The comments contained in this letter reflect the input of the Committees and PCUA staff.

Credit unions are mutually owned cooperatives that deliver retail financial services to their member owners. Credit unions operate not-for-profit and they do not issue capital stock. Consistent with our democratic ownership structure, credit unions support financial transparency. To that end, we support identifying impairments to assets in a timely manner, accurate reporting of any such impairment and the provision for adequate or properly funded allowance accounts. Such measures enhance safety and soundness and protect the interests of our member/owners.

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### *Impairment Generally*

In response to the Supplementary Document, we question whether adoption of the proposed impairment model truly enhances the mechanisms for detection of impairments and the building of adequate allowances. Currently, federally insured credit unions (shares/deposits insured by the National Credit Union Share Insurance Fund) adhere to Interpretive Ruling and Policy Statement (IRPS) 02-3 promulgated by the National Credit Union Administration (NCUA). The NCUA has made minor adjustments to IRPS 02-3 over the years. However, the major guides for identifying impairments and providing for an allowance for loan losses are Statement of Financial Accounting Standards (FAS) No. 5 and No. 114.

The Supplementary Document does not distinguish FAS 5 or FAS 114 in terms of whether the proposed impairment model replaces those standards. Nor does the Supplementary Document make any arguments to the effect that FAS 5 or 114 are insufficient to achieve the ends of an adequately funded allowance. Accordingly, it would be prudent for FASB to extend the comment period for further analysis of any perceived weaknesses to the current model for reporting impairments and funding an allowance account. Future consideration should also address the relative merits of the Supplementary Document in comparison and contrast to FAS 5 and 114. FASB should also articulate whether the approach outlined in the Supplementary Document is replacing current standards and any phase-in or timing for compliance with the proposed new model.

### *Open Portfolio*

Technically, the definition of the term “open portfolio” is reasonable. That said, we urge FASB to further consider whether the application of the open portfolio concept enhances the adequacy of reporting impairments or funding an allowance in a material manner in connection with the consumer and business lending conducted by credit unions.

In 2010, Pennsylvania’s credit unions generated \$19.5 billion in loans. Those totals break down as: 28.44% first mortgage; 26.28% other real estate; 25.72% automobile; 7.85% unsecured credit card; 6.69% other unsecured; 4.43% other; and 0.59% non-real estate business.<sup>1</sup> Of the roughly \$5.5 billion worth of first mortgages originated, 41.15% was sold on the secondary market. One can reasonably conclude that the consumer and business lending portfolio of Pennsylvania credit unions is a traditional and conservative pool of assets.

In addition to a traditional or conservative approach to lending, all financial institution regulators, including the NCUA are scrutinizing risk activities. Through our membership, PCUA has reason to know that at the supervisory and examination level risk areas such as concentrations, underwriting standards, real estate or collateral values and the adequacy of the allowance for loan losses are undergoing heightened review. The Boards and management teams of credit unions are redoubling risk management efforts.

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<sup>1</sup> Source of data is Callahan’s Peer to Peer, which aggregates information from reports of financial condition filed with the NCUA.

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FASB should take note of the emerging legal and regulatory environment connected to consumer lending as it undertakes its final analysis of the Supplementary Document. Pending laws and regulations will further reduce the risk profile of lending activities. Here is a sampling:

- Title XIV of the Dodd-Frank Act constitutes a massive overhaul of the Truth-in-Lending Act, some provisions of the Real Estate Settlement Procedures Act and other laws relevant to mortgage lending. These amendments go beyond enhancing consumer disclosures. The new rules dictate, to some extent, the terms and conditions of credit.
- Between 2007 and the current date, the Federal Reserve has finalized numerous amendments to Regulation Z which implements the Truth-in-Lending Act. These changes, too, regulate the terms and conditions of consumer credit.
- NCUA recently release for comment a proposed rule or guidance for managing interest rate risk.

The point in cataloguing credit union lending activity and the changes in laws that apply to consumer credit is to illustrate that a new environment exists for consumer and business credit underwriting. More disclosures as well as more care and scrutiny of credit facilities will continue to take place at the onset of the credit relationship. While underwriting is not an inoculation from defaults or impairments, FASB should take note that a reduce risk profile now exists. With that in mind, the policy and practical implications remain: will the proposed open portfolio/ impairment model generate significantly more transparent balance sheets and safer and sounder allowance provisions than the current approach. We assert that the benefit of the newer model does not outweigh the compliance burdens to execute it.

#### *Compliance Consequences, Impact on Net Worth*

Federally insured credit unions with assets greater than \$10 million must adhere to generally accepted accounting principles (GAAP) for financial reporting purposes. Further, they must satisfy a net worth maintenance regime known as Prompt Corrective Action (PCA). 12 USCA § 1790d, 12 C.F.R. Part 702, 17 P.S. § 513. It bears repeating that credit unions are non-profit, mutually owned financial cooperatives that do not issue capital stock. Credit unions build net worth through set-asides of retained earnings. Pursuant to PCA, once a federally insured credit union's net worth ratio (a ratio of net worth to total assets) dips below 7%, it must respond to an increasingly strict scheme of supervisory enforcement actions aimed at restoring the net worth ratio.

The Supplementary Document with its strictures of a "good book" and a "bad book," paints a cloudy picture, at best, of how to implement the model and its corresponding impact on a credit union's net worth. In a credit union, net worth as well as an allowance account is funded from current earnings. Credit union net worth is under stress due to current economic conditions. Conformity to the Supplementary Document, if finalized, should not come at the expense of a credit union's net worth ratio. To be clear, a credit union or any other institution confronting

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impairments should address those in an appropriate fashion and address the consequences. But, again, a federally insured credit union should not suffer a compliance burden, particularly one as severe as compliance with PCA due to a change in the methodology for addressing impairments.

*Good Book and Bad Book*

In short, the Committees suggest that FASB offer further definition of the concepts of good book and bad book. It appears unclear what loans should be reported in either book. The proposal raises the question of whether an asset can be transferred between the good book or bad book. Without further clarification, uniform application of the model will not be possible. It also raises the specter or potential for disagreement between the institution, its private auditors and prudential regulator over appropriate reporting of impairment and the adequacy of the allowance account.

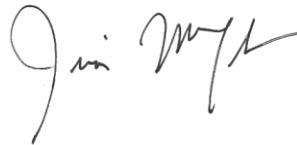
*Conclusions*

Consistent with our commitment to transparency and accurate reporting, credit unions would tend to support accounting standards for impairment that dramatically enhance safety and soundness. Based on the Supplementary Document, we are not in a position to conclude that the proposed guidelines for impairment represent a marked improvement over FAS 5 and FAS 114. The financial services industry remains under stress. Changing the rules for reporting impairment at this time creates too much potential for negative compliance consequences that outweigh any notional benefits to changing the approach.

We would be happy to address the comments addressed in this letter with FASB at your convenience.

Very truly yours,

PENNSYLVANIA CREDIT UNION ASSOCIATION



James J. McCormack  
President/CEO

cc: PCUA Board  
Regulatory Review Committee  
State Credit Union Advisory Committee  
M. Dunn, CUNA