September 7, 2010

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

Via email to director@fasb.org

Reference: File Reference No. 1830-100, Proposed Accounting Standards Update,  
Fair Value Measurements and Disclosures (Topic 820): Amendments for Common  
Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs

Dear Mr. Golden:

Freddie Mac appreciates the opportunity to comment on the Exposure Draft for the Proposed Accounting Standards Update of Topic 820, Fair Value Measurements and Disclosures (Topic 820): Amendments for Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs (the “proposed Update”).

Freddie Mac was chartered by Congress in 1970 with a mission to increase the availability of funds for home ownership by developing and maintaining a secondary market for residential mortgages. We participate in the secondary mortgage market principally by providing our credit guarantee on the mortgage-related securities we issue, and investing in mortgages and mortgage-related securities. We hold a significant amount of financial assets and liabilities measured at fair value on a recurring or nonrecurring basis. As of June 30, 2010, our consolidated balance sheet reflects $317 billion of financial assets and $8.62 billion of financial liabilities measured at fair value; $135.76 billion (42.82%) of these financial assets and $0.05 billion (0.58%) of these financial liabilities are classified as Level 3 financial instruments in the fair value hierarchy.

We fully support the Board’s efforts to develop common requirements for measuring fair value and for disclosing information about fair value measurements under both U.S. GAAP and International Financial Reporting Standards (“IFRSs”). We commend the Board for attempting to develop a converged standard and addressing constituents comments and recommendations relating to the measurement and disclosure of fair values.
However, as discussed below, we have several concerns with the guidance in the proposed Update.

**Conceptual conflict with fair value definition and impracticability of measurement uncertainty analysis**

We do not agree with the requirement to disclose a measurement uncertainty analysis of the effects of reasonably possible alternative unobservable inputs for recurring fair value measurements categorized within Level 3 of the fair value hierarchy.

We believe that the required disclosure will not present meaningful information about an entity’s risk exposure and will represent a significant operational burden for entities that employ a significant number of valuation models/techniques in determining their Level 3 fair value measurements. Furthermore, we believe the cost to develop these disclosures will far outweigh the expected benefits to users of financial statements. Please refer to our response to Question 7, which addresses this concern in greater detail.

**Lack of consistent principle for the consideration of an entity’s specific decisions regarding financial instruments in fair value measurements**

We believe the proposed Update lacks a consistent principle for considering an entity’s specific decisions regarding the fair value measurement of financial instruments. We do not understand the conceptual merit of permitting consideration of an entity’s specific decisions related to groups of financial instruments managed on the basis of net exposure to a market risk, financial assets representing a control premium or discount, or thinly traded instruments, but prohibiting consideration of an entity’s specific decision related to block discounts. Please refer to our responses to Questions 4, 5, and 6 for additional details regarding this concern.

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The views expressed in this comment letter are solely those of Freddie Mac, and do not purport to represent the views of the Federal Housing Finance Agency, as Conservator.

Our detailed comments on the concerns summarized above are discussed in Appendix A for the Board’s consideration. We have also responded to some of the individual questions posed by the Board in the proposed Update and have included these responses in the attached Appendix A.

Freddie Mac appreciates the opportunity to provide our comments on the proposed Update. If you have any questions about our comments, please contact Timothy Kviz (703-714-3800) or James Brandt (703-714-3305).
Sincerely,

Robert D. Mailloux
Senior Vice President – Corporate Controller and Principal Accounting Officer

cc: Mr. Charles E. Haldeman, Jr., Chief Executive Officer
    Mr. Ross J. Kari, Executive Vice President – Chief Financial Officer
    Ms. Wanda I. DeLeo, Senior Associate Director and Chief Accountant, Federal Housing Finance Agency
Appendix A

This Appendix includes our responses and comments to the specific questions raised by FASB in the proposed Update.

Question 1: This Exposure Draft represents the Board’s commitment toward developing common fair value measurement guidance with the IASB. Do you think the proposed amendments:

a. Would improve the understandability of the fair value measurement guidance in U.S. GAAP? If not, why not?

b. Would result in any unintended consequences on the application of the proposed amendments? If so, please describe those consequences.

Response:

a. We believe that, other than the items discussed in our response to questions 4, 5, 6, and 7, the proposed amendments will improve the understandability of the fair value measurement guidance in U.S. GAAP.

b. We think that, except for the proposed measurement sensitivity analysis disclosure discussed in our response to question 7, the proposed amendments will not result in any unintended consequences on the application of the proposed changes.

Question 2: The Board has decided to specify that the concepts of highest and best use and valuation premise are only to be applied when measuring the fair value of nonfinancial assets. Are there situations in which those concepts could be applied to financial assets or to liabilities? If so, please describe those situations.

Response: We agree with the Board that the concepts of highest and best use and valuation premise are not relevant for measuring the fair value of financial assets or of financial liabilities. We agree with the Board’s view, expressed in paragraph BC26 of the proposed Update, that “the accounting for financial instruments should provide information about the risks inherent in financial instruments on the basis of how a reporting entity manages its business so that users of financial statements can assess the amounts, timing, and uncertainty of future cash flows.”

Question 3: Do you agree with the proposed guidance for measuring the fair value of an instrument classified in shareholders’ equity? Why or why not?

Response: We agree with the proposed guidance for measuring the fair value of an instrument classified in shareholders’ equity as an estimate of an exit price from the perspective of a market participant who holds the instrument as an asset at the measurement date. We believe the proposed guidance would improve the consistency in application of fair value measurement guidance to instruments classified in shareholders’ equity among various entities.
Question 4: The Board has decided to permit an exception to fair value measurement requirements for measuring the fair value of a group of financial assets and financial liabilities that are managed on the basis of the reporting entity’s net exposure to a particular market risk (or risks) (that is, interest rate risk, currency risk, or other price risk) or to the credit risk of a particular counterparty.
   a. Do you think that proposal is appropriate? If not, why not?
   b. Do you believe that the application of the proposed guidance would change the fair value measurements of financial assets and financial liabilities that are managed on the basis of the reporting entity’s net exposure to those risks? If so, please describe how the proposed guidance would affect current practice.

Question 5: The Board has decided to clarify the meaning of a blockage factor and to prohibit the use of a blockage factor when fair value is measured using a quoted price for an asset or a liability (or similar assets or liabilities). Do you think that proposal is appropriate? If not, why not?

Question 6: The Board has decided to specify that other premiums and discounts (for example, a control premium or a non-controlling interest discount) should be taken into account in fair value measurements categorized within Level 2 and Level 3 of the fair value hierarchy when market participants would take into account those premiums or discounts when pricing an asset or a liability consistent with the unit of account for that asset or liability.
   a. Do you think that proposal is appropriate? If not, why not?
   b. When the unit of account for a particular asset or liability is not clearly specified in another Topic, how would you apply that proposed guidance in practice? Please describe the circumstances (that is, the asset or liability and the relevant Topic) for which the unit of account is not clear.

Response: We believe these questions highlight the lack of a consistent principle in the proposed Update for considering an entity’s specific decisions regarding financial instruments in fair value measurements. Specifically, the Board expressly permits consideration of an entity’s specific decisions for groups of financial assets and liabilities managed on the basis of a net exposure to a market risk, for transactions that would involve a control premium or discount, and when an instrument is thinly traded; however, the Board expressly prohibits an entity’s specific decisions as it relates to block discounts. We do not understand the conceptual merit for the exception for block discounts. Further, we note that adjustments for thinly traded securities and adjustments for blocks are economically equivalent. We suggest that the Board develop a principle that can be consistently applied to how an entity’s specific decisions should be considered in a fair value measurement.

That being said, we believe that an entity’s specific decisions should be taken into consideration in fair value measurements in certain circumstances. As articulated in paragraph BC26 of the proposed Update, “the accounting for financial instruments should provide information about the risks inherent in financial instruments on the basis of how

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A reporting entity manages its business so that users of financial statements can assess the amounts, timing, and uncertainty of future cash flows” (emphasis added). We believe that fair value measurements that are representative of an entity’s business strategy are more useful to a user of the financial statements. Thus, an entity’s specific decisions may be relevant to a fair value measurement.

Question 7: The Board has decided to require a reporting entity to disclose a measurement uncertainty analysis that takes into account the effect of correlation between unobservable inputs for recurring fair value measurements categorized within Level 3 of the fair value hierarchy unless another Topic specifies that such a disclosure is not required for a particular asset or liability (for example, the Board has decided in its project on the accounting for financial instruments that a measurement uncertainty analysis disclosure would not be required for investments in unquoted equity instruments). Do you think that proposal is appropriate? If not, why not?

Response: We strongly disagree with the proposed requirement to provide a measurement uncertainty analysis for financial instruments classified as Level 3 in the fair value hierarchy due to the following reasons:

- The proposed Update does not provide sufficient clarity on what is meant by “reasonably possible alternative unobservable inputs.” This may lead to diversity in practice due to varying interpretations of what these alternative unobservable inputs might be (e.g., based on bid-ask spreads, stress tests, possible scenarios, value-at-risk analyses, etc.). This diversity in practice would result in reduced comparability across entities in the fair value measurement process.

- Freddie Mac holds a significant number of financial instruments classified in the Level 3 fair value measurement hierarchy, representing approximately 20 classes of its financial assets and liabilities. Disclosing the sensitivity analysis by class would significantly increase the volume of information about the fair value of financial instruments provided in our financial statements. We believe the volume of information required to be disclosed around the sensitivity analysis for entities with a significant number of financial instruments classified within Level 3 might be too obscure and voluminous to be meaningfully consumed by a financial statement user. Additionally, the level of disaggregation required by the proposed ASU is not consistent with the way we view or manage the business. We view and manage risks inherent in our portfolio in aggregate. For the assets and liabilities we manage based on fair value, we do not make any distinction between the levels of the fair value hierarchy. The levels of the fair value hierarchy are only important relative to required financial statement disclosures. Given that the disclosures required by the proposed ASU are not consistent with how we view or manage our business, it is not clear to us how providing disaggregated information about a portion of our portfolio would be useful to a financial statement users.

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We believe that obtaining the supporting information necessary to construct this disclosure would represent a significant operational burden for entities with a significant volume of financial assets and liabilities in Level 3 of the fair value hierarchy. We also note that financial assets and liabilities that are valued based upon third-party quotes or pricing services may present unique challenges for disclosing the required information.

We have over 3,200 CUSIPs in our non-agency mortgage-backed debt securities portfolio measured at fair value each period and classified as Level 3 of fair value hierarchy due to significant unobservable inputs used in the fair value measurements. Due to the large volume of securities that we own, we utilize multiple independent pricing services to obtain fair values. These independent pricing services generally provide prices based on observed transactions in the marketplace for similar securities extrapolated to meet the specific characteristics of our securities.

More specifically, we send individual CUSIPs to four independent pricing services. We use the median of all the reasonable fair values provided. We subject this fair value to verification procedures by requesting dealer quotes from two or three dealers for a sample of these securities. In addition, we perform a series of analytical reviews including trend and relative value analysis to validate the reasonableness of the fair values provided by the pricing services and hold discussions with pricing services and dealers to ensure that we understand their overall extrapolation and valuation techniques.

We are unsure how we could reliably determine reasonably possible alternative inputs when pricing is extrapolated using observed trades for similar assets, which is the case for much of the pricing provided by pricing services. When pricing is extrapolated from observed trades rather than discounted cash flow or other models, alternative values cannot be obtained simply by increasing or decreasing a significant unobservable input for the cash flow model such as the discount rate, prepayment speeds, or credit loss assumptions. To comply with requirements of the proposed Update, we would need to have our independent pricing services provide us with additional prices for reasonably possible alternative unobservable inputs for each asset and liability that we categorize in Level 3. Since each pricing service may use different techniques and models to estimate fair value of these securities, there may be inconsistency as to which inputs are significant.

We believe it is possible that the various independent pricing services and dealers we use to derive our fair value measurements could derive significantly different fair values based on their view of reasonably possible alternative inputs. We are not certain how we would reconcile or consume the output received from external pricing sources. Reconciliation of the various values given the difference in view about reasonably possible alternative inputs would be unwieldy.
• Even if we could overcome our operational constraints, we believe the presentation of alternative amounts undermines the Balance Sheet presentation of our best estimate of fair value amounts. Based on our due diligence and related internal controls, we have provided our best estimate of what we could receive for our assets or to transfer our liabilities for in an orderly transaction with a market participant. The current proposal would provide a financial statement reader with a range of values from which to choose, instead of one value determined based on the principles of ASC 820-10.

• We believe the cost to implement sensitivity analysis disclosure would outweigh the expected benefits to users of financial statements. The disclosure requirements as stated in the proposed Update would require entities to incur significant costs to develop and implement system and model enhancements, infrastructure, processes, and internal controls to prepare the new disclosures. These disclosure requirements would also likely result in expanding reporting entities’ to expand their use of third-party pricing services at additional cost.

If the Board decides to retain the fair value measurements sensitivity disclosure as currently proposed, we would encourage the Board to consider providing additional implementation guidance surrounding the determination of “unobservable input amounts that could have reasonably been used” to ensure consistent application of this disclosure standard across entities.

*Question 8: Are there alternative disclosures to the proposed measurement uncertainty analysis that you believe might provide users of financial statements with information about the measurement uncertainty inherent in fair value measurements categorized within Level 3 of the fair value hierarchy that the Board should consider instead? If so, please provide a description of those disclosures and the reasons why you think that information would be more useful and more cost-beneficial.*

*Response:* We believe that additional qualitative disclosure of fair value models, methodologies, techniques, and unobservable inputs used in determination of fair value measurements of Level 3 fair value hierarchy by class of financial assets and liabilities, including the discussion of the effect of correlation between unobservable inputs, would be more meaningful and useful to users of financial statements. Such disclosure could provide detailed information about the subjectivity and uncertainty of Level 3 fair value measurements and let users of financial statements assess the sensitivity of such fair value measurements to changes in unobservable inputs based on their understanding and view of reasonably possible alternative inputs, the economic environment and market risks relevant to such instruments.

Additional qualitative disclosure would be a more cost-effective alternative to measurement uncertainty analysis as it would be less costly and burdensome to implement for entities, regardless of the level of sophistication of the models and processes used to determine Level 3 fair value measurements. The alternative of expanded qualitative disclosure also would provide meaningful information about
sensitivity of Level 3 fair value measurements to changes in unobservable inputs that we believe will be easier for users of financial statements to understand.

**Question 9: The Board has decided to require limited retrospective transition. Do you think that proposal is appropriate? If not, why not?**

**Response:** We believe limited retrospective transition for the proposed Update is appropriate considering the effect of the proposed amendments on the current practice of fair value measurements and disclosures.

**Question 10: There is no link to the transition guidance for the proposed amendments that the Board believes would not change practice. Are there any proposed amendments that are not linked to the transition guidance that you think should be linked? If so, please identify those proposed amendments and why you think they should be linked to the transition guidance.**

**Response:** We believe there are not any proposed amendments that would change current practice for fair value measurements that are not linked to the transition guidance. We believe no additional links are required.

**Question 11: The amendments in this proposed Update would apply to public and nonpublic entities (that is, private companies and not-for-profit organizations). Should any of the proposed amendments be different for nonpublic entities? If so, please identify those proposed amendments and describe how and why you think they should be different.**

**Response:** We believe that the proposed amendments should not be different for nonpublic entities as they build upon the fair value measurements and disclosures required by entities under the provisions of Topic 820, which have been in place for several years.

We are a significant user of financial statements, as we review the financial statements of our business partners, including seller/servicers, mortgage insurers, bond insurers, and other credit enhancement providers, as part of our evaluation of our counterparty credit risk and the operating performance of our business partners. In performing review and analysis of financial statements, we would not find different disclosures meaningful simply because an entity was public or nonpublic. Further, differences in disclosures provided by public versus private entities would impair our ability to analyze and compare the financial statements across entities.

**Question 12: How much time do you think constituents would need to prepare for and implement the amendments in this proposed Update?**

**Response:** As discussed in our response to question 7, the measurement uncertainty disclosure requirement of the proposed Update would present numerous implementation challenges, in part due to lack of clarity on what is meant by a reasonably possible alternative inputs and the lack of guidance for determining the effects of reasonably
possible alternative inputs of fair values when third-party pricing services are used. Depending on clarification and additional guidance for these questions, the implementation of this disclosure might require significant time and resources to augment our current fair value measurement models, methodologies, systems, process, procedures, and controls. Therefore, it is difficult to provide a precise estimate on the time period necessary to implement this disclosure requirement. Depending on whether further clarification is provided (and the ultimate guidance that is issued), we may need anywhere from six months to two years to implement the amendments to the proposed Update.

We do not expect the other proposed amendments to require an extended implementation period. With the exception of the measurement uncertainty disclosure, we believe that one year would be sufficient time to implement the other amendments proposed in this proposed Update.